FOR THE FISCAL YEAR ENDED MARCH 31, 1999 | PUBLISHED IN SEPTEMBER 1999

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# TREASURY ANNUAL REPORT

Alberta
TREASURY

# Treasury Annual Report 1998-99

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# PREFACE

## PUBLIC ACCOUNTS 1998-99

The Public Accounts of Alberta are prepared in accordance with the Financial Administration Act and the Government Accountability Act. The Public Accounts consist of the annual report of the Government of Alberta and the annual reports of each of the 18 Ministries.

The annual report of the Government of Alberta released in June contains the Provincial Treasurer's accountability statement, the consolidated financial statements of the Province and a comparison of the actual performance results to desired results set out in the government's business plan, including the *Measuring Up* report.

This annual report of the Ministry of Treasury contains the Minister's accountability statement, the audited consolidated financial statements of the ministry and a comparison of actual performance results to desired results set out in the ministry business plan. This Ministry annual report also includes:

- the financial statements of entities making up the ministry including the Department of Treasury, regulated funds, provincial agencies and Crown-controlled corporations for which the Minister is responsible,
- other financial information as required by the Financial Administration Act and Government Accountability Act, either as separate reports or as part of the financial statements, to the extent that the ministry has anything to report,
- financial information relating to trust funds, and
- the report of the auditor of the Office of the Auditor General included in the annual report of the Auditor General, which is hereby incorporated in the Public Accounts by reference.

# MINISTER'S ACCOUNTABILITY STATEMENT

The Ministry's Annual Report for the year ended March 31, 1999 was prepared under my direction in accordance with the Government Accountability Act and the government's accounting policies. All of the government's policy decisions as at August 31, 1999 with material economic or fiscal implications of which I am aware have been considered in the preparation of the Ministry Annual Report.

Stockwell Day
Provincial Treasurer

August 31, 1999

# A MESSAGE FROM THE PROVINCIAL TREASURER

## RESPONSIBLE FINANCIAL MANAGEMENT AND LOW TAXES

Volatile is the only way to describe the global fiscal climate during the 1998-99 fiscal year. Instability in financial markets all over the world and dramatic fluctuations in commodity prices (particularly oil) made balancing our provincial budget more challenging than any other time in recent history.

Despite the volatility, Alberta's economy remained steady and strong during the 1998-99 fiscal year. Of course, Albertans and their hard work are responsible for these excellent results. However, it is this government that is responsible for creating a fiscal environment that gives Albertans the ability and the confidence to do the work that has made Alberta an economic leader in Canada.

The Ministry of Treasury helped to keep the provincial government on track with business planning during the year. With the introduction of the Fiscal Responsibility Act, sound and scrupulous financial practices are legislated throughout government. Moreover, our prudent forecasting ensured that core services were funded at optimum levels in 1998-99 while allowing us to pay down over $1 billion of the province's accumulated debt and all-but-eliminating the net debt. We can now focus our full attention on paying down the remaining accumulated debt, which stands at $14.1 billion.

In turn, the relatively rapid pay-down of debt contributed greatly to our now premium credit rating, further lowering our cost for borrowing money. Alberta's cost of borrowing was the lowest of all the provinces in 1998-99.

With our economy on solid footing and the continual improvements to our financial management systems, we gave ourselves room to move in the area of taxes. Tax reforms we announced in March will give us freedom to create tax policy unique in Canada, by unhooking our personal provincial income taxes from federal taxes. We will also increase personal and spousal deductions to a level where 78,000 low-income Albertans will no longer have to pay any provincial income tax.

In fact, when combined with other recently implemented reforms, this plan will allow Albertans at every income level to keep more of what they earn. When fully implemented the plan will save Albertans more than $600 million each year.

During 1998-99, the staff at Alberta Treasury have been invaluable, carrying out this government's financial plans to the letter. I congratulate them on the results they've achieved not only on behalf of the Ministry, but also on behalf of all Albertans. As we all continue to work together for the people of Alberta, we look forward to reporting on the successes undoubtedly achievable in the coming year as we continue to stay our prudent fiscal course while lowering taxes.

Stockwell Day
Provincial Treasurer

August 31, 1999

# MANAGEMENT'S RESPONSIBILITY FOR REPORTING

The executives of the individual entities within the ministry have the primary responsibility and accountability for the respective entities. Collectively, we ensure the ministry complies with all relevant legislation, regulations and policies.

Ministry business plans, annual reports, performance results and the supporting management information are integral to the government's fiscal and business plans, annual report, quarterly reports and other financial and performance reporting.

Responsibility for the integrity and objectivity of the consolidated financial statements and performance results for the ministry rests with the Provincial Treasurer. Under the direction of the Provincial Treasurer, I oversee the preparation of the ministry's annual report, including the consolidated financial statements and performance results. The consolidated statements and the performance results, of necessity, include amounts that are based on estimates and judgements. The consolidated financial statements are prepared in accordance with the government's stated accounting policies.

As Deputy Provincial Treasurer, in addition to program responsibilities, I establish and maintain the ministry's financial administration and reporting functions. The ministry maintains systems of financial management and internal control which give consideration to costs, benefits, and risks that are designed to:

- provide reasonable assurance that transactions are properly authorized, executed in accordance with prescribed legislation and regulations, and properly recorded so as to maintain accountability of public money,
- provide information to manage and report on performance,
- safeguard the assets and properties of the Province under ministry administration,
- provide Executive Council, Treasury Board and the Provincial Treasurer any information needed to fulfil their responsibilities, and
- facilitate preparation of ministry business plans and annual reports required under the Government Accountability Act.

*The Ministry of Treasury includes:*

- *Department of Treasury*
- *Alberta Heritage Foundation for Medical Research Endowment Fund*
- *Alberta Heritage Savings Trust Fund*
- *Alberta Heritage Scholarship Fund*
- *Alberta Risk Management Fund*
- *Utility Companies Income Tax Rebates Fund*
- *Alberta Insurance Council*
- *Alberta Municipal Financing Corporation*
- *Alberta Pensions Administration Corporation*
- *Alberta Securities Commission*
- *The Alberta Government Telephones Commission and its subsidiaries*
- *Alberta Treasury Branches and its subsidiary*
- *Credit Union Deposit Guarantee Corporation*
- *N.A. Properties (1994) Ltd.*
- *S C Financial Ltd.*
- *Chembiomed Ltd.*
- *Gainers Inc.*

In fulfilling my responsibilities for the ministry, I have relied, as necessary, on the executives of the individual entities within the ministry.

Peter Kruselnicki, P.Eng.
Deputy Provincial Treasurer

# OPERATIONAL OVERVIEW

# OPERATIONAL OVERVIEW

Treasury oversees government performance measures and financial management and reporting. Treasury is responsible for budget planning and management, intergovernmental fiscal arrangements, tax policy, tax administration, economic analysis, statistics, public pensions, and administrative and financial services regulation.

### TREASURY'S GOALS FOR 1998-99

1. A healthy and sustainable financial position.
2. An accountable government.
3. A fair, competitive, and simple provincial tax system managed efficiently and effectively.
4. Investment returns maximized and borrowing costs minimized subject to acceptable risk.
5. An efficient, fair and competitive capital market and an efficient and fair regulatory environment for financial institutions.
6. Quality financial services to Albertans through Alberta Treasury Branches, Alberta Municipal Financing Corporation and Alberta Pensions Administration Corporation.

### TREASURY'S CORE BUSINESSES

1. Provide analysis and recommendations to the Provincial Treasurer and Treasury Board.
2. Maintain a framework that fosters government accountability.
3. Administer and collect tax revenue.
4. Manage the province's financial assets and liabilities.
5. Foster a fair and efficient financial marketplace.
6. Provide financial services through Alberta Treasury Branches, Alberta Municipal Financing Corporation and Alberta Pensions Administration.

### TREASURY'S MISSION

*To provide excellence in financial management, services and advice to achieve a healthy and sustainable financial condition for the province with the lowest possible taxes for Albertans.*

## HIGHLIGHTS

- For the fifth year in a row, the budget was balanced and a payment was made to reduce the province's net debt. Forward looking business planning and prudent forecasting helped the province pay down $1.03 billion of the net debt, before pension provisions. As a result, the province's net debt will be eliminated in 1999-2000 and the province can now focus its full attention on reducing the accumulated debt, which stands at $14.1 billion.
- A new tax plan, to be phased in over the next three years, was announced. When fully implemented in 2002, there will be a single tax rate of 11% based on taxable income rather than the basic federal tax. The "temporary deficit elimination" flat tax and surtax will be eliminated. Basic personal and spousal exemptions will increase substantially, to $11,620. Bracket creep will also be eliminated. The new tax system will result in annual tax savings of $600 million for Albertans, with an additional 78,000 low income Albertans being removed from the tax rolls.
- Railway fuel tax dropped from 6 cents a litre to three cents a litre effective January 1, 1999.
- Treasury continued to report, on a timely and user friendly basis, to Albertans regarding the province's finances and the government's progress in achieving its performance targets.
- Standard and Poor's upgraded Alberta's credit rating to AA+, the highest among provinces. Alberta borrows at the lowest average interest-rate spread of any Canadian province.
- The Heritage Savings Trust Fund had a net income of $932 million in 1998-99, down from $947 million the previous year. The Fund's net assets were $12 billion.
- Alberta Treasury Branches earned a net profit of $111 million, substantially better than its forecast of $46 million.

# TREASURY'S OPERATIONAL STRUCTURE

## OFFICE OF BUDGET AND MANAGEMENT

The Office of Budget and Management (OBM) manages the provincial budget and business plan review and approval process, prepares economic and fiscal forecasts, and provides research analysis and recommendations on the province's fiscal, economic, taxation and pension policies. OBM is responsible for intergovernmental fiscal relations and for providing statistical information about the province. It also proposes and prepares accounting and financial control policies, prepares budget documents, quarterly forecasts, quarterly and annual financial statements, and performance measurement reports.

## TAX AND REVENUE ADMINISTRATION

Revenue collection and administration is the responsibility of Tax and Revenue Administration (TRA). TRA works closely with the Tax Policy group of the Office of Budget and Management on matters of tax policy and legislation. Together the two areas work towards providing a fair, competitive, simple and efficient provincial tax revenue system.

## INVESTMENT MANAGEMENT

Investment Management works to maximize investment returns for the province within an acceptable degree of risk. It provides investment expertise to a wide range of provincial government entities including the Alberta Heritage Savings Trust Fund, the Alberta Heritage Scholarship Fund and the Alberta Heritage Foundation Medical Research Endowment Fund. It also administers $20 billion in trust funds, the bulk of which are the public sector pension funds sponsored by the province.

## LIABILITY MANAGEMENT

Liability Management works to achieve the lowest cost on debt within an acceptable degree of variability on debt servicing costs. Alberta meets its borrowing requirements through a number of borrowing programs that allow the province to lower debt costs and diversify its investor base. Various financial products and instruments are employed to meet debt management objectives.

## TREASURY OPERATIONS

Treasury Operations is responsible for back office support for investment and liability management; risk management services for the government; monitoring and managing loans and guarantees; and regulation of the financial institution industry in Alberta.

## REGULATORY AGENCIES

Annual Reports detailing the operations and results of the Alberta Securities Commission, the Credit Union Deposit Guarantee Corporation, the Alberta Insurance Council and the Alberta Automobile Insurance Board are available from the respective regulatory agency.

## FINANCIAL SERVICES

Treasury provides financial services through Alberta Treasury Branches, Alberta Municipal Financing Corporation and the Alberta Pensions Administration Corporation.

## RELATIONSHIP OF TREASURY REPORTING ENTITIES TO GOALS

**Alberta Treasury**

Ministry Support Services

### Goal 1
A healthy and sustainable financial position

**Treasury Department**
- Office of Budget and Management
- Treasury Operations (Risk Management and Insurance) (Alberta Risk Management Fund)

### Goal 2
An accountable government

**Treasury Department**
- Office of Budget and Management

### Goal 3
A fair, competitive, and simple provincial tax system managed efficiently and effectively

**Treasury Department**
- Tax and Revenue Administration
- Office of Budget and Management (Tax Policy)

**Funds**
- Utility Companies Income Tax Rebates Fund*

### Goal 4
Investment returns maximized and borrowing costs minimized, subject to acceptable risk

**Treasury Department**
- Liability Management
- Treasury Operations
- Investment Management

**Funds**
- Alberta Heritage Foundation for Medical Research Endowment Fund
- Alberta Heritage Savings Trust Fund
- Alberta Heritage Scholarship Fund

### Goal 5
An efficient, fair and competitive capital market and an efficient and fair regulatory environment for financial institutions

**Treasury Department**
- Treasury Operations

**Provincial Agencies**
- Alberta Insurance Council
- Alberta Securities Commission

**Commercial Enterprises**
- Credit Union Deposit Guarantee Corporation
  - SC Financial Ltd.

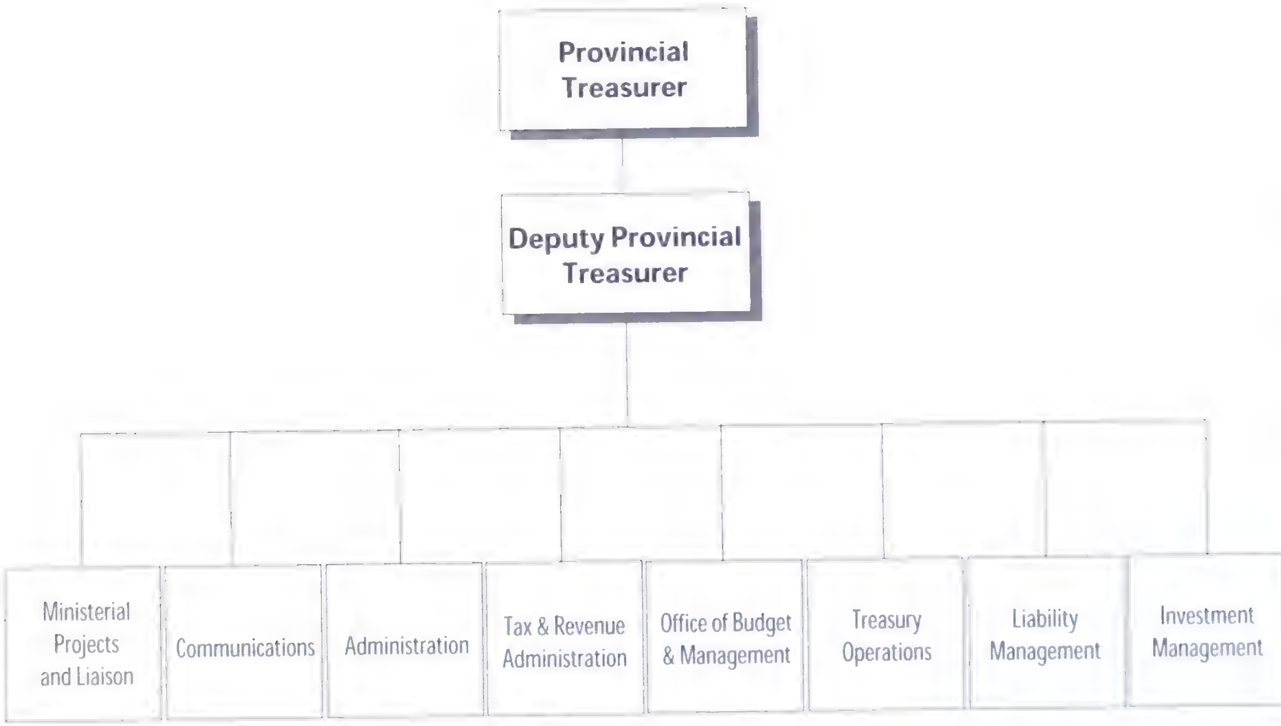
### Goal 6
Quality financial services to Albertans through Alberta Treasury Branches, Alberta Municipal Financing Corporation, and Alberta Pensions Administration Corporation

**Provincial Agencies**
- Alberta Pensions Administration Corporation

**Commercial Enterprises**
- Alberta Government Telephones Commission
  - 475342 Alberta Ltd.*
  - NFI Finance, Inc.*
- Alberta Intermodal Services Ltd.*
- Alberta Municipal Financing Corporation
- Alberta Treasury Branches
- N.A. Properties (1994) Ltd.

**Crown-Controlled Corporations**
- Chembiomed Ltd.*
- Gainers Inc.*

* These entities are in wind-up


Provincial Treasurer
Deputy Provincial Treasurer
Ministerial Projects and Liaison
Communications
Administration
Tax & Revenue Administration
Office of Budget & Management
Treasury Operations
Liability Management
Investment Management

## TREASURY EXECUTIVE OR CHIEF OPERATING OFFICERS AND MEMBERS OF BOARDS, COUNCILS AND COMMISSIONS
as at March 31, 1999

| Entity | Executive | Board, Council or Commission Members |
|---|---|---|
| **Alberta Treasury** | Al O'Brien, *Deputy Provincial Treasurer*<br>Peter Kruselnicki, *Associate Deputy Provincial Treasurer*<br>Jim Peters, *Controller*<br>Robert Bhatia, *Assistant Deputy Provincial Treasurer - Treasury Operations*<br>Len Rokosh, *Assistant Deputy* Provincial Treasurer - *Revenue*<br>Stan Susinski, *Chief Investment Officer*<br>Michael Faulkner, *Corporate Secretary*<br>Alex Fowlie, *Ministerial Projects and Liaison*<br>Shannon Taylor, *Acting Director - Communications* | |
| **Credit Union Deposit Guarantee Corporation** | Jim Laitner, *Chief Executive Officer* | Bob Splane, *Chair*<br>Mary Arnold, *Vice-Chair*<br>Bob Campbell<br>Ron Gilmore<br>John Henry<br>Rod McDermand<br>Al O'Brien |
| **Alberta Municipal Financing Corporation** | Terrance Stroich, *General Manager* | Allister McPherson, *Chair and Treasurer*<br>Jim Drinkwater<br>Del Dyck<br>Rob Feddema<br>Eric McGhan<br>Don Lussier<br>Al O'Brien<br>Garth Sherwin<br>Bob Splane |

## TREASURY EXECUTIVE OR CHIEF OPERATING OFFICERS AND MEMBERS OF BOARDS, COUNCILS AND COMMISSIONS
as at March 31, 1999

| Entity | Executive | Board, Council or Commission Members |
| --- | --- | --- |
| Alberta Pensions Administration Corporation | George Buse, *Chief Operating Officer* | Jack McMahon, *Chair*<br>Ted Barnicoat<br>Allan Habstritt<br>Rick Milner<br>Al O'Brien<br>Len Pederson<br>Richard West |
| Alberta Securities Commission | | William Hess, *Chair*<br>Eric Spink, *Vice-Chair*<br>James Allard<br>Jerry Bennis<br>Wendy Best<br>John Cranston<br>Ian McConnan<br>Walter O'Donoghue<br>Thomas Pinder<br>Thomas Shields |
| Alberta Treasury Branches | Paul Haggis, *Chief Executive Officer and Superintendent* | Marshall Williams, *Chair*<br>Robert Brawn<br>Garth Griffiths<br>Brian Heidecker<br>Brian Hesje<br>David Hughes<br>Diane Hunter<br>Ian Macdonald<br>Elson McDougald<br>Garnett Millard<br>Raymond Nelson<br>Ralph Scurfield<br>Gail Surkan<br>Ron Triffo |

## TREASURY EXECUTIVE OR CHIEF OPERATING OFFICERS AND MEMBERS OF BOARDS, COUNCILS AND COMMISSIONS
as at March 31, 1999

| Entity | Executive | Board, Council or Commission Members |
|---|---|---|
| Alberta Insurance Council | Joanne Abram, *General Manager* | Neil Miller, *Chair*<br>Greg Empson<br>Mike Hirst<br>Betty Johnson<br>Jack Laverick |
| Alberta Automobile Insurance Board | | John Tweddle, *Chair*<br>Paul Galway<br>W. Harry Gough<br>Patricia Hryniw |
| General Insurance Council | | Randy McDonald, *Chair*<br>Guy Bourgeois<br>Jeff Cuell<br>Rod Garraway<br>Maree Hall<br>Bill Lausen<br>Neil Miller<br>Melvin Niebrugge |
| Insurance Adjusters Council | | Jack Laverick, *Chair*<br>Dennis Anderson<br>Mike Hirst<br>Gavin Lane |
| Life Insurance Council | | Norman Chandler, *Chair*<br>Lynne Arling<br>Ted Hanna<br>David Hicks<br>Duncan McLachlan<br>Ray Wold |

## TREASURY EXECUTIVE OR CHIEF OPERATING OFFICERS AND MEMBERS OF BOARDS, COUNCILS AND COMMISSIONS
as at March 31, 1999

| Entity | Executive | Board, Council or Commission Members |
| --- | --- | --- |

Provincial Treasurer Stockwell Day is the trustee of pension plan funds and is responsible for appointing pension plan governing boards which have been established as follows:

| Entity | Executive | Board, Council or Commission Members |
| --- | --- | --- |
| Local Authorities Pension Plan | | Richard West, *Chair*<br>Kenneth Balkwill<br>Rick Blakeley<br>Ben Boettcher<br>Terry Cavanagh<br>Margaret Johnson<br>Tony Krivoblocki<br>Richard Martin<br>Elaine Noel-Bentley<br>William Purdy<br>Carl Soderstrom<br>Janis Tarchuk<br>Sandra Weidner<br>Leslie Young |
| Management Employees Pension Board | | Jack Phelps, *Chair*<br>Robert Algar<br>Fred Barth<br>Shirley Howe<br>Dianne Keefe<br>Tony Morehen<br>Theresa Ostrum |
| Public Service Pension Plan Board | | Len Pederson, *Chair*<br>Jim Campbell<br>Virendra Gupta<br>Ian Tarr<br>Tim Wiles |

## TREASURY EXECUTIVE OR CHIEF OPERATING OFFICERS AND MEMBERS OF BOARDS, COUNCILS AND COMMISSIONS
**as at March 31, 1999**

| Entity | Executive | Board, Council or Commission Members |
|---|---|---|
| Special Forces Pension Plan Board | | Allan Habstritt, *Chair*<br>David Carpenter<br>Colin Catonio<br>Harvey Cenaiko<br>Ulysses Currie<br>Randell Garvey<br>Janina Vanderpost |
| Universities Academic Pension Plan Board | | Keith Winter, *Chair*<br>Jeremiah Allen<br>Ronald David Bercov<br>Auke Elzinga<br>Gary Frey<br>Virendra Gupta<br>Mary Hamilton<br>Glenn Harris<br>Ted Horbulyk |

## ACTS ADMINISTERED BY TREASURY
**as at March 31, 1999**

Alberta Corporate Tax Act
Alberta Heritage Savings Trust Fund Act
Alberta Income Tax Act
Alberta Municipal Financing Corporation Act
Alberta Securities Commission Reorganization Act
Alberta Taxpayers Protection Act
Alberta Treasury Branches Act
Appropriation Acts
Balanced Budget and Debt Retirement Act
Civil Service Garnishee Act
Credit Union Act
Farm Credit Stability Act
Financial Administration Act
Financial Consumers Act
Fiscal Responsibility Act
Fuel Tax Act
Government Accountability Act
Hotel Room Tax Act
Insurance Act
Loan & Trust Corporations Act
Lottery Fund Transfer Act
Members of the Legislative Assembly Pension Plan Act
Municipal Debentures Act
Pension Fund Act
Public Sector Pension Plans Act
Reinvestment Act
Securities Act
Small Business Term Assistance Act
Statistics Bureau Act
Telecommunications Act (Part I)
Tobacco Tax Act
Utility Companies Income Tax Rebates Act

# REPORT OF THE AUDITOR GENERAL ON THE RESULTS OF APPLYING SPECIFIED AUDITING PROCEDURES TO KEY PERFORMANCE MEASURES

**TO THE MEMBERS OF THE LEGISLATIVE ASSEMBLY:**

I have performed the following procedures in connection with the Ministry of Treasury's key performance measures included in the *Treasury Annual Report for the fiscal year ended March 31, 1999* presented on pages 24, 32, 36, 39 and 47.

1. Information obtained from an independent source was agreed with the information supplied by the stated source. Information provided internally was agreed to the reports from the systems used to develop the information.

2. The calculations which converted source information into reported measures were tested.

3. The appropriateness of the description of each measure's methodology was assessed.

As a result of applying the above procedures, I found no exceptions. However, these procedures do not constitute an audit of the key performance measures and therefore I express no opinion on the key performance measures included in the *Treasury Annual Report for the fiscal year ended March 31, 1999.*

Peter Valentine

FCA
Auditor General
Edmonton, Alberta

July 30, 1999

# RESULTS ANALYSIS

# RESULTS ANALYSIS

The Department of Treasury achieved many successes over the 1998-99 year. The ministry met or exceeded most of the performance targets identified in its business plan which was published in *Budget '98.*

### REVENUE HIGHLIGHTS

- Personal income tax revenue increased by $724 million in 1998-99 as a result of a 3.4% increase in employment and a 2.3% increase in the average wage in Alberta. Corporate income taxes decreased by $190 million. This can be attributed to low commodity prices and, particularly, oil which fell from an average of US$19 per barrel in 1997-98 to a 12 year low of under US$11 per barrel in December of 1998.
- Investment income decreased $157 million. The decline was due mainly to lower capital gains, lower interest rates and foreign exchange losses.
- Insurance corporation tax receipts decreased by $20 million, primarily as a result of an adjustment arising from the estimate in the 1997-98 Public Accounts being higher than amounts subsequently received.
- Taxes from tobacco increased $11 million, attributable both to an increase in Alberta's population and to a higher consumption rate.
- Fuel tax revenues decreased by $11 million. There was a 20% increase in the amount of rebates for tax-exempt fuel users and a one-time remission of $6 million to a group of bulk fuel dealers with respect to the sale of marked fuel.
- Alberta Treasury Branches profits increased by $25 million in 1999. The main reasons for the improvement were continued low loan loss provisions and continuing strong net interest margins of 3.2%.

### FINANCIAL RESULTS

*Revenues for the Ministry in 1998-99 were $8,878 million. This was up $361 million or 4.2% from 1997-98. Expenses in 1998-99 were $1,958 million, up $168 million or 9.4% from the previous fiscal year. The net result was that revenues exceeded expenses by $6,920 million. This was $193 million more than 1997-98 and was also $913 million more than budgeted.*

*"Because there are traces of taxpayers' sweat in every dollar this government spends, we must spend wisely, on the things that matter most."*

STOCKWELL DAY
PROVINCIAL TREASURER

**EXPENSE HIGHLIGHTS**

- Debt servicing costs for provincial purposes increased $83 million from 1997-98, due to the fluctuation in the value of the Canadian dollar relative to the U.S. dollar. For municipal, hospital and school purposes, debt servicing costs decreased $40 million due to lower interest rates and to an overall decline in the size of the loan portfolio during the year.
- Corporate tax interest refunds increased $80 million over the previous year due to a one-time payment on a large claim.
- Valuation adjustments increased $75 million from 1997-98. This was a result of lower gains on pension provisions, offset by lower losses on doubtful accounts and loans.
- In 1998-99, financial management and planning expenses came in $19 million less than the previous year. This change was due mainly to the absence of activities related to the Principal Group settlement.

GOAL 1

# A HEALTHY AND SUSTAINABLE FINANCIAL POSITION

## BALANCED BUDGET AND DEBT RETIREMENT

The Alberta government posted its fifth consecutive surplus in 1998-99. Forward looking business planning, responsible economic and fiscal policies and prudent forecasting helped the province achieve a consolidated debt payment, excluding pension provisions of just over one billion dollars for the year ended March 31, 1999.

The province eliminated its net debt in June 1999 and can now focus on the remaining accumulated debt. The new Fiscal Responsibility Act developed by Treasury will ensure the orderly pay down of accumulated debt over the next 25 years. The new act requires that three-quarters of the legislated economic cushion of 3.5% of revenue and of any revenue increases during the year must be applied to pay down the debt.

**ALBERTA'S CONSOLIDATED SURPLUS (EXCLUDING PENSION PROVISIONS)**
Surplus (Deficit) in millions of dollars

| | 1993-94 | 1994-95 | 1995-96 | 1996-97 | 1997-98 | 1998-99 |
|---|---|---|---|---|---|---|
| Target | (2,500) | (1,800) | (800) | 0 | 100 | 100 |
| Budget | (2,171) | (1,550) | (506) | 23 | 154 | 165 |
| Actual | (1,384) | 958 | 1,132 | 2,527 | 2,639 | 1,026 |

The 1998-99 surplus of $1,026 million excluding pension provisions exceeded the budgeted surplus of $165 million by $861 million. Actual revenues of $16,922 million exceeded budgeted revenue by $1,645 million due primarily to higher than budgeted income tax revenue, investment income and net income from commercial operations. Actual expenses excluding pension provisions exceeded budgeted expenses by $784 million primarily due to higher than budgeted expenses for priority areas such as health.

*"Even in the face of considerable challenges, our economic performance in Alberta has been solid this year, keeping us on track to eliminate the net debt."*

STOCKWELL DAY
PROVINCIAL TREASURER
FEBRUARY 22, 1999

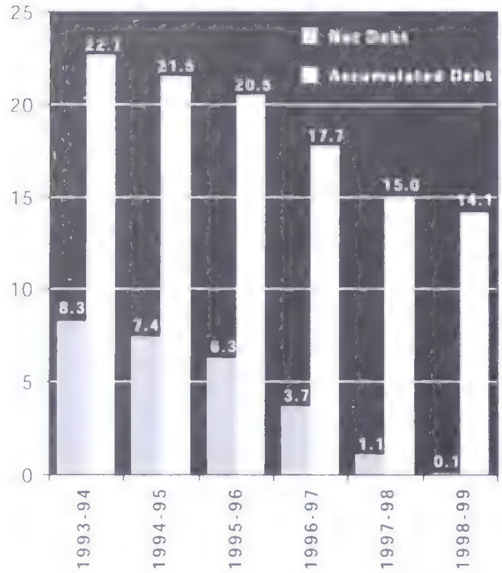
*How do you spell diversification?*

*In Alberta, economic diversification is akin to economic stability. The effects of our growing diversification are clearly evident in 1998's economic results. We took in 37% less oil revenue than the year before, yet our economy grew by 3.1% and employment was up by 3.9%, or 57,100 jobs. In Alberta, diversification spells relief.*

Key Performance Measure

**DEBT RETIREMENT WELL AHEAD OF TARGET**

Net Debt versus Accumulated Debt




Net debt has decreased dramatically over the past five years from \$8.3 billion at March 31, 1994 to a net debt of only \$63 million at March 31, 1999. Responsible and prudent stewardship of Alberta's resources through budget and business planning processes eliminated the net debt in June 1999, ten years ahead of schedule.

In recognition of Alberta's strong fiscal performance, Standard and Poor's announced the Province's second straight AA+ credit rating. Alberta has the highest credit rating of any Canadian province, which helps give us the lowest cost of borrowing among the provinces.

**CREDIT RATING**

| | Alberta | British Columbia | Ontario |
|---|---|---|---|
| March 31, 1999: | | | |
| Standard and Poor's | AA+ | AA | AA |
| Moody's | Aa1 | Aa2 | Aa3 |

Moody's Investors Service upgraded Alberta's Canadian dollar debt from Aa2 to Aa1 on June 14, 1999. The rating reflects the expectation of continued debt reduction and strong budget performance.

## BUSINESS PLANNING, ECONOMIC AND FISCAL POLICIES AND FORECASTING

Treasury co-ordinates the government's overall business planning process through:

- providing accounting advice and developing accounting and financial control policies for use across government,
- developing standards for ministry and departmental financial statements, and assisting ministries in preparing their financial statements,
- developing key government-wide performance measures,
- assisting ministries to improve their business plan performance measurement systems,
- developing standards for ministry annual reports,
- reviewing ministries' annual business plan submissions and ministry annual reports, and
- developing, with each ministry, program spending options and identifying reallocation opportunities to help ensure that fiscal targets are met.

As responsible stewards of Alberta's finances, Treasury provides advice and support to the Provincial Treasurer and Treasury Board. Treasury also co-ordinates the overall government business plan, including key government-wide performance measures.

During 1998-99, Treasury led the government's 1999-2002 fiscal and business plan process and prepared *Budget '99*. Treasury develops common economic and financial assumptions for business planning across government. The department monitors achievement of business plan goals and establishes standards and policies for overall government. The Treasury Department is always looking for ways to refine the business planning process including streamlining administration by eliminating unnecessary regulation and duplication.

The annual survey of ministries was modified from the 1997 survey to include two additional categories. Somewhat satisfied and very dissatisfied were added to the previous four categories of very satisfied, satisfied, somewhat dissatisfied and dissatisfied. Based on the two new categories, 66% of the responding ministries were satisfied or very satisfied with the advice, support and recommendations provided by Treasury. A further 18% were somewhat satisfied.

## FEDERAL-PROVINCIAL FISCAL ARRANGEMENTS

Treasury strives to ensure that Albertans are treated equitably by the federal government. The department develops and presents Alberta's position on federal-provincial fiscal arrangements to the federal government, including working with other provinces. Treasury's goal is to ensure that Alberta's per capita cash from the federal Canada Health and Social Transfer (CHST) is equal to other provinces. During 1998-99, Treasury contributed to reforming federal-provincial arrangements resulting in an increase of nearly $200 million in CHST revenues starting in 1999-2000 and an accelerated process of moving to equal per capita allocation of the CHST transfer.

## PENSION POLICY

During 1998-99, Treasury's and the pension boards' excellent management of the government's pension obligations had a direct impact on Alberta achieving the best credit rating of all provinces in Canada. At March 31, 1999 the government's pension liabilities were $4.8 billion, a decrease of $77 million from the previous year. Most public sector pension plans are reaching fully funded status. During the year, the Local Authorities Pension Plan became fully funded resulting in a savings of $11 million in 1998. Treasury is working with the pension plan boards in order to facilitate the move of the Local Authorities Pension Plan and the Universities Pension Plan towards non-statutory status.

## RISK MANAGEMENT SERVICES

Through the Risk Management Fund, Treasury helps ministries protect public assets from the risk of accidental loss, reduces the cost of administering risk management services, and ensures accountability of ministries and agencies. During 1998-99, the Risk Management Fund recorded a surplus of $7.2 million. This results from contributions of $6.1 million from the Department of Treasury relating to the Fund's pre-April 1995 deficit. As a result, the Fund's accumulated deficit was reduced to $1.4 million as at March 31, 1999.

In 1998-99, a survey of senior financial officers indicated that 100% of ministries were satisfied with the risk management and insurance services provided by Treasury.

GOAL 2

# AN ACCOUNTABLE GOVERNMENT

Alberta continues to be a leader in government financial reporting. Treasury provides Albertans with regular reports on goals, performance measures and financial results. A comprehensive report on both financial and program results is provided to Albertans on the results achieved compared to targets set in the Government Business Plan.

The Government Accountability Act requires the annual publication of three-year budget and business plans in the annual budget that identify goals, objectives and financial plans of the government and individual ministries. The Act also requires that the government provide quarterly financial updates and an annual report on both financial and performance results. Treasury co-ordinates the preparation of these publications.

Other laws require balanced budgets, elimination of Alberta's net debt, improved accountability for results, taxpayer protection and an end to special government loans and loan guarantees to business.

*"Alberta continues to lead the way in comprehensive reporting, not just on the financial side, but also on the performance side, measuring our results and tracking progress against the goals we set."*

STOCKWELL DAY,
PROVINCIAL TREASURER

## CONSOLIDATED BUDGETS AND BUSINESS PLANS

Alberta publishes consolidated budgets and business plans for all government entities. *Budget '98* included the 1998-2001 Business Plan and Fiscal Plan, a description of the Alberta Advantage, an Economic Overview and a Tax Plan. It established goals and measures for each of the government's core businesses. A comprehensive set of strategies and actions to achieve these goals was outlined in the various ministry business plans.

As required by the Government Accountability Act, the 1998-99 Annual Report of the Government of Alberta, *Agenda for Opportunity,* which was published June 1999, provided an accounting of government-wide financial results and performance measures in comparison to the plans set out in *Budget '98.* Ministry measures are provided in the annual report of each ministry, which also must include ministry consolidated financial statements and financial statements of each of the components of the ministry.

## MEASURING AND REPORTING THE GOVERNMENT'S PERFORMANCE

The 1998-99 Annual Report of the Alberta government also included *Measuring Up*, the fifth annual report on the performance of the Government of Alberta. The report provides the public with an accountability document that compares results achieved to targets set in the Government Business Plan. In addition, *Measuring Up* reported on the government's strategies to illustrate what is being done to achieve its goals.

*Measuring Up* contains core measures that are related to government goals. Measuring and tracking results make it possible for policy makers to improve the quality of programs and services for Albertans and to help make choices about whether to revise, retain, or abandon existing programs.

## TREASURY'S INTERACTION WITH MINISTRIES

Treasury provides leadership in accountability for financial management. Ministries have the responsibility for reporting financial results and business outcomes at the Ministry level. Treasury's role is to monitor and advise, rather than maintain financial controls. Treasury also prepares the Province's consolidated financial statements based upon the ministry financial statements.

Treasury has retained overall responsibility for setting government accounting policies, but it involves the ministries in the development of these policies and standards. Ministries are responsible for managing their financial affairs in accordance with these policies.

## SATISFACTION WITH TREASURY'S PERFORMANCE

Treasury undertakes client satisfaction surveys annually. One survey measures the public satisfaction and another measures the satisfaction of deputy ministers with the government's accountability system.

The deputy ministers' survey was modified from the 1997 survey to include two additional categories. Somewhat satisfied and very dissatisfied were added to the previous four categories of very satisfied, satisfied, somewhat dissatisfied and dissatisfied. Based on the two new categories 70% of the responding deputies were very satisfied or satisfied, below Treasury's target of 80% satisfied or very satisfied. 30% were somewhat satisfied with the government accountability system.

A September 1998 survey indicated that 69% of Albertans knew that the government had a surplus in the previous year. A further 12% believed the government broke even. The target is for 80% of Albertans to be aware of the province's financial performance.

### AUDITOR GENERAL'S SATISFACTION WITH THE GOVERNMENT'S ACCOUNTABILITY SYSTEM

In his 1997-98 Annual Report, the Auditor General stated that "Treasury continued to make significant improvements to accountability reporting in 1997-98."

The Auditor General has recommended the Ministry of Treasury make the following changes:

- Initiate changes to the corporate government accounting policies in order to eliminate the reservations in auditor's reports on department and ministry financial statements.
  - ✓ Partially accepted. In some cases, plans are underway to address the matter. In other cases, it requires further review (e.g., timing of recognition of certain grants).
- Develop a methodology to allocate all significant costs to the entities responsible for delivering outputs.

  The Auditor General has stated that aspects of allocation require further study. Consideration should be given to the potential benefits and appropriate mechanisms for allocation of the net book value of capital assets currently owned by central agencies, such as the Department of Public Works, Supply and Services, and the cost of capital, based on the assets employed by individual entities in delivering services.
  - ✓ Accepted in principle. A key issue in addressing this recommendation is to consider methods that align responsibility to manage costs with cost allocation.
- Develop strategies to improve year-end reporting processes for ministries and their agencies.
  - ✓ Treasury agrees with this recommendation and activities are already underway.

- Consolidated financial statements should be prepared in accordance with generally accepted accounting principles for the summary financial statements of government by, for example, including the financial results of post-secondary institutions and regional health authorities.
  - ✓ Accepted in principle. A review of this issue is ongoing. It is not clear whether expanding the reporting entity is expected by the public or if it would add value to our financial reporting, or be the best practice.
- Report the actual results to date for revenues, expense and surplus on the accrual basis in the quarterly report's Consolidated Fiscal Summary.
  - ✓ Treasury agrees and full accrual accounting practices were adopted in 1998-99.
- Develop a business plan for Investment Management Division.
  - ✓ Agreed and a draft business plan has been prepared.

GOAL 3

## A FAIR, COMPETITIVE AND SIMPLE PROVINCIAL TAX SYSTEM MANAGED EFFICIENTLY AND EFFECTIVELY

The Government remains committed to strengthening the Alberta Advantage and building on its successes. Deficits have been eliminated and a legislated plan to repay the accumulated debt is in place. We have an affordable, effective and accountable government. Specific plans are being made to reduce taxes and leave more money in the hands of individual Albertans.

*A new tax plan for Albertans announced*

- Major changes to the personal tax system will be phased in over the next three years. When fully implemented in 2002, there will be a single tax rate of 11% based on taxable income rather than the basic federal tax. The "temporary deficit elimination" flat tax and surtax will be eliminated. Basic personal and spousal exemptions will increase substantially to $11,620. Albertans will continue to file only one tax return.
- The new tax system will result in tax savings of $600 million per year, with an additional 78,000 low income Albertans being removed from the tax rolls.
- The Alberta Family Employment Tax Credit, introduced in 1997, doubled in 1998. About 160,000 low and middle income working families with children received credits of up to $1,000 for the year.
- Railway fuel tax dropped from six cents to three cents per litre on January 1, 1999.

One of the key performance measures used as a standard to compare how Alberta is performing relative to the other provinces is a comparison of the total tax load on Albertans to that of people living in other provinces. In 1998-99, Albertans paid the lowest total taxes, meeting one of Treasury's key performance targets.

Low taxes encourage people to work, save and invest and stimulate job creation as new businesses are created and existing business expand. This is reflected in Alberta's impressive employment performance in 1998. Alberta created 51,600 jobs between December 1997 and December 1998. In only two years, Alberta is almost two-thirds of the way towards achieving Treasury's four-year job creation target of 155,000 jobs. Alberta's employment participation rate was 72% in 1998, the highest in Canada and more than six percentage points greater than the national average.

**Key Performance Measure**

**LOWEST TAX LOAD IN CANADA: PROVINCIAL TAXES PAYABLE* BY A FAMILY OF FOUR**

(Two Children Families) 1999

| | One-income Family earning $30,000 | Two-income Family earning $55,000 | Two-income Family $100,000 |
|---|---|---|---|
| Alberta | $1,629 | $3,846 | $8,194 |
| Ontario | $2,324 | $4,763 | $10,128 |
| British Columbia | $2,723 | $5,249 | $10,364 |
| Nova Scotia | $2,850 | $5,294 | $11,412 |
| New Brunswick | $3,034 | $5,357 | $11,752 |
| Saskatchewan | $3,236 | $5,524 | $11,955 |
| Prince Edward Island | $3,478 | $5,860 | $12,440 |
| Manitoba | $2,878 | $5,899 | $13,377 |
| Newfoundland | $4,292 | $7,230 | $15,028 |
| Quebec | $1,888 | $7,596 | $18,026 |

* Includes provincial income, sales, payroll, provincial tobacco and fuel taxes and health care premiums

***Source:*** Alberta Treasury

***Note:*** Assumptions for calculations can be found in *Budget '99*, page 134

**SECOND LOWEST BASIC PERSONAL TAX RATE IN CANADA - 1999**

| Province | % of Basic Federal Tax | Province | % of Basic Federal Tax |
|---|---|---|---|
| Ontario | 40.5% | Nova Scotia | 57.5% |
| Alberta | 44.0% | Prince Edward Island | 59.5% |
| Saskatchewan | 48.0% | New Brunswick | 60.0% |
| British Columbia | 49.5% | Newfoundland | 69.0% |
| Manitoba | 50.0% | Quebec | Not comparable |

***Source:*** Alberta Treasury

## SECOND LOWEST TAXES ON BUSINESS

Alberta has the second lowest tax load on businesses among provinces, just behind Nova Scotia. Our target is to have the lowest overall business taxes in Canada. Our low business taxes are encouraging new business start-ups and other businesses to move to our province. In 1998-99, 30,970 new businesses were registered, a 49% increase over 1997-98.

**Key Performance Measure**

**PROVINCIAL TAX LOAD ON BUSINESS - 1998-99**

| | | | |
|---|---|---|---|
| Nova Scotia | 74.3 | Manitoba | 102.2 |
| Alberta | 76.1 | Ontario | 102.3 |
| New Brunswick | 81.2 | British Columbia | 121.0 |
| Prince Edward Island | 90.5 | Newfoundland | 127.0 |
| Quebec | 95.8 | Saskatchewan | 155.7 |

Tax Load relative to provincial average = 100.0

***Source:*** Department of Finance Canada

### FINANCIAL INSTITUTIONS CAPITAL TAX

Legislation was passed during the spring sitting which harmonizes the provincial tax base for the financial institutions capital tax with the tax base for the federal large corporations tax. The rate was reduced to ensure that the change was revenue neutral. This change, which had been requested by the industry, will make it easier for them to calculate the tax and complete required forms.

### ALBERTA ROYALTY TAX CREDIT PROGRAM

A review of the entire program is currently being undertaken. It is expected a new program will be in place by 2001.

### ADVANCES IN THE USE OF TECHNOLOGY

Tax and Revenue Administration (TRA) is constantly working on technological advances to increase its efficiency and effectiveness. The goal is to reduce the time it takes and the amount it costs for individuals and businesses to provide the information required by TRA. Initiatives currently in place and those being contemplated include:

- using Interactive Voice Response (IVR) to file liquid propane gas tax refund claims. This technology will be utilized for filing hotel room tax returns in the near future,
- maximizing the use of imaging technology to simplify records management and providing for easier and faster retrieval of documents,
- allowing pre-authorized debits for payment of taxes and instalments,
- changes to the agreement with the Canadian Payments Association to allow tax and instalment payments to be made at any bank in Canada,
- expanded use of the Treasury Internet site to include more forms and publications,
- e-filing of corporate income tax returns, a joint project with Revenue Canada and the Ontario Ministry of Finance (an official launch date will be announced in early 2000), and
- the development by TRA, in conjunction with Treaty Seven First Nations, of a "smart card" which will include information identifying the cardholder as being eligible for the Alberta Indian Tax Exemption on personal use fuel and tobacco. This will also simplify reporting requirements for businesses selling to eligible customers.

### FUEL TAX UNIFORMITY

Alberta is working closely with industry, Revenue Canada and the other provinces on the Fuel Tax Uniformity Project. A uniform fuel tax return and schedules are now in place. As well, agreement was reached on a common standard for fuel dye, which is providing significant benefits to industry and some benefit to government.

### CALGARY OFFICE

TRA has moved its Calgary office to a better location to provide improved service to taxpayers of southern Alberta. This will establish a more visible presence in Calgary and enable taxpayers residing there to have face-to-face accessibility.

### Y2K READINESS

Computer systems are being upgraded from mainframe to client-server technology. This will ensure not only that all systems are Y2K compliant, but will provide for e-filing of corporate returns, improve TRA's assessment processing efficiency and also establish the platform necessary for future electronic data interchange and electronic commerce. Systems will be ready or workarounds in place before December 31, 1999. TRA anticipates there will be no interruption in service to clients.

### CLIENT SURVEY AND PERFORMANCE MEASUREMENT

The annual client survey conducted by TRA showed some promising results. In 1997, the overall average satisfaction rate with the administration of Alberta's tax programs was 78.1%. For 1998, different questions were posed to those surveyed. The response to the question in which those surveyed were asked whether the services provided by TRA were equal to or better than those of other tax administrations resulted in a satisfaction level of 80.1%. With respect to the amount it costs taxpayers to comply with the particular program, the satisfaction index rose to 74% from 70.9%. The targets remain at 85% for the satisfaction with tax administration, and 80% for the satisfaction with compliance costs. New initiatives are expected to raise the satisfaction level on both targets in the medium term.

While clients are becoming more satisfied with their compliance costs, the cost for TRA to process a return or claim decreased from $82 in 1997-98 to $76 in 1998-99.

GOAL 4

# INVESTMENT RETURNS MAXIMIZED AND BORROWING COSTS MINIMIZED SUBJECT TO ACCEPTABLE RISK

## LIABILITY MANAGEMENT

Liability Management works to achieve the lowest cost on debt within an acceptable degree of variability on debt servicing costs. Alberta meets its borrowing requirements through a number of borrowing programs that allow the province to lower debt costs and diversify its investor base. Various financial products and instruments are employed to meet debt management objectives.

During 1998-99, Treasury issued several medium-term notes in the Canadian market, one global note and two European medium-term notes. The department also completed several financings for provincial corporations.

During the year, Treasury continued efforts to provide information to credit rating agencies and investors in Alberta bonds. These initiatives included:

- providing detailed briefings and continual updates on the province's financial and economic status to credit rating agencies,
- producing The Alberta Advantage, which provides financial information on the province,
- making presentations to investment banks, life insurance companies, and pension funds that invest in Alberta bonds, and
- maintaining a database of over 200 investors and analysts throughout the world, who were sent budget highlights and other financial information.

### Performance Measures

Treasury has established a benchmark portfolio which is used to measure the performance of the province's debt portfolio. The benchmark debt portfolio was developed with the assistance of major international investment banks. The 1998-99 benchmark portfolio had the following composition: duration of Canadian dollar debt of 2.8 years (approximately a 3.5 year term to maturity); duration of U.S. dollar debt of 1.0 years (approximately a 1.1 year term to maturity); and the proportion of U.S. dollar debt is similar to that of the province's actual debt portfolio. Duration is the weighted average term to maturity of a

bond, or portfolio of bonds, that takes into account the timing and amount of both principal and interest payments.

### 1. Total cost of debt

- This measures the total cost of carrying the debt portfolio, including cash interest costs and change in the market value of debt outstanding.
- The market value cost of debt is calculated using the industry-standard time-weighted method. This measure reflects the economic cost of the debt and incorporates changes in the value of Alberta bonds due to changes in interest rates.
- This cost is compared to the market value cost of debt of the benchmark portfolio. The market value cost of Alberta's debt should be less than or equal to the cost of the benchmark portfolio.
- Overall, the market value cost of debt for the province's portfolio was lower than the benchmark portfolio. The Canadian dollar portion of the portfolio out-performed the benchmark, the result of a portfolio structure designed to take advantage of falling interest rates in 1998-99. The cost of the U.S. dollar portion of the portfolio, in Canadian dollars, matched the benchmark's performance.

**Key Performance Measure**
**MARKET VALUE COST OF DEBT**
Year Ended March 31, 1999

| | Alberta Debt Portfolio % | Benchmark Portfolio % |
|---|---|---|
| Canadian Dollar Portfolio | 5.9 | 6.1 |
| U.S. Dollar Portfolio (in Canadian dollars) | 12.8 | 12.8 |
| **Total Portfolio in Canadian Dollars** | **8.3** | **8.5** |

### 2. Market Spreads

- Alberta's cost of borrowing is determined relative to the federal government interest rate for the same term. The federal government enjoys a higher credit rating than the provinces owing to its greater taxing power.
- The difference in the interest rate Alberta would pay on a particular term debt compared to what the federal government would pay is the market spread. The relative market spread for comparable provinces is a reflection of the province's credit rating as well as the market's perception of the province's fiscal and debt management.
- Alberta has borrowed at the lowest market spreads of any Canadian province in every year since 1994-95, achieving the target set out in Treasury's 1998-99 business plan.

MARKET SPREADS

| | 5-year Bonds | | | | 10-year Bonds | | | |
|---|---|---|---|---|---|---|---|---|
| | Canada | Alberta | B.C. | Ontario | Canada | Alberta | B.C. | Ontario |
| | Rate (%) | (basis point spread)* | | | Rate (%) | (basis point spread)* | | |
| March 31, 1995 | 8.37 | +11 | +13 | +30 | 8.67 | +17 | +19 | +36 |
| March 31, 1996 | 7.05 | + 8 | +10 | +17 | 7.67 | +14 | +17 | +28 |
| March 31, 1997 | 6.04 | + 5 | +11 | +11 | 6.68 | +8 | +18 | +18 |
| March 31, 1998 | 5.26 | + 7 | +13 | +13 | 5.42 | +13 | +22 | +20 |
| March 31, 1999 | 5.30 | +13 | +24 | +19 | 5.09 | +19 | +33 | +27 |

* A basis point is one one-hundredth of a percentage point

## 3. Credit Rating Agencies

Treasury's goal is to ensure that credit rating agencies understand the province's financial and economic position. In a survey of credit rating agencies, all reported being satisfied or very satisfied on 28 out of 32 questions regarding the effectiveness of briefings provided.

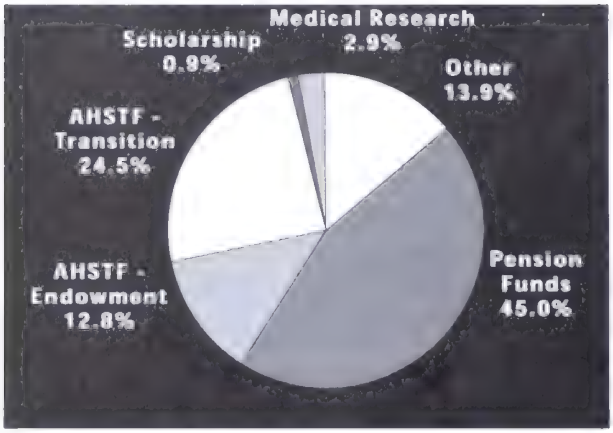
### INVESTMENT MANAGEMENT

The Investment Management Division (IMD) was established to act as the investment manager for pools of capital assigned by statute to the Provincial Treasurer and where specific agreements have been made with provincial public sector bodies to act as an investment advisor. IMD's objective is to create portfolios of assets that match established risk profiles and financial goals of the funds under management. In addition, IMD provides market information to the Provincial Treasurer as required.

The Investment Operations Committee was established in 1997-98 to add private sector financial and business oversight to the Investment Management Division's (IMD) investment operations and results. The Investment Operations Committee is chaired by the Deputy Provincial Treasurer and consists primarily of private sector members. The committee also has the responsibility to review and make recommendations with respect to the Alberta Heritage Savings Trust Fund.

With $34 billion under management at the end of fiscal 1998-99, IMD is responsible for one of the largest pools of investment capital in Canada. With this large pool of capital, investment management services can be provided on an efficient and cost effective basis. IMD has a staff of 38 investment professionals. Many of the staff have advanced university degrees and 11 have received their Chartered Financial Analyst designation, a recognized standard of investment expertise in the industry.

ASSETS UNDER MANAGEMENT BY IMD




Of the $34 billion in assets under management, the Alberta Heritage Savings Trust Fund represents $12 billion and $15 billion consists of public sector pension funds. Other funds managed by IMD include the Consolidated Cash Investment Trust Fund and funds managed on behalf of The Workers' Compensation Board, the Alberta Heritage Scholarship Fund and the Alberta Heritage Foundation for Medical Research Endowment Fund.

The investment objectives vary for the funds under management reflecting different financial requirements and risk tolerances for each fund and the fund stakeholders. To meet the investment policies and achieve the goals of each fund, IMD has developed a wide range of investment products, which can be put together to meet each fund's specific risk profile. To accomplish this, both IMD and third party external manager expertise are used. This ensures the necessary specialized knowledge and skills are utilized. External managers are used primarily when investing in foreign equities and in specialized domestic areas.

There were three significant developments that affected IMD during the 1998-99 fiscal year. Firstly, the province re-organized the funding of its long-term disability benefit obligations to civil servants. The Provincial Treasurer received the authority to make investments on behalf of the two Long Term Disability Benefit Funds so as to achieve a higher long-run rate of return on assets. Prior to this re-organization, these obligations were dealt with on a pay-as-you-go basis.

Secondly, an Order-in-Council was passed that gave the Provincial Treasurer the authority to manage pension funds that may no longer be sponsored by statute. Some public pension funds are considering being

sponsored outside of government statute. The Order-in-Council allows the Provincial Treasurer to continue to manage these fund assets, pursuant to an agreement between the fund and the Treasurer.

Finally, as part of its continuing objective to improve the investment products available to the various fund sponsors, IMD hired three new investment management firms to make equity investments in large capitalized publicly traded Canadian companies. These firms were hired on the basis of their differing investment styles, thus allowing IMD to offer the client funds the ability to diversify their investments in Canadian equities.

The overall performance of the investment products by asset class managed by IMD is shown in the following table.

**Key Performance Measure**
**INVESTMENT PERFORMANCE OF MARKETABLE POOLS**
For the Year Ended March 31, 1999

| Pool Size | Description of Pool | Annual Return (%) | Benchmark Return* (%) | Benchmark Index (Total Return) |
|---|---|---|---|---|
| Consolidated Cash Investment Trust Fund ($1,979 million) | Money Market | 5.2% | 4.9% | ScotiaCapital Markets 91-Day Treasury Bill Index |
| Canadian Public Debt Pool ($8,113 million) | Canadian Debt | 7.5% | 7.0% | ScotiaCapital Markets Bond Universe Index |
| Domestic Passive Equity Pool ($2,008 million) | Canadian Equity Index Fund based on the TSE 300 | -11.1% | -11.3% | Toronto Stock Exchange 300 Index |
| Domestic Structured Equity Pool ($215 million) | Canadian Equity Structured Product based on the TSE 100 | -11.0% | -11.3% | Toronto Stock Exchange 100 Index |
| Canadian Pooled Equity ($2,042 million) | Actively Managed Canadian Equity Fund | -7.6% | -11.3% | Toronto Stock Exchange 300 Index |
| Canadian Small Cap Pool ($437 million) | Actively Managed Canadian Equity Fund Focused on Smaller Capitalized Companies | -18.4% | -21.3% | Nesbitt Burns Small Cap Index |
| Global Structured Equity Pool ($1,379 million) | Foreign Equity Structured Product based on MSCI World Index | 12.5% | 19.8% | MSCI World Index ($Cdn.) |
| Foreign Equity Managers Pool ($3,743 million) | Actively Managed Foreign Equity Funds | 18.2% | 19.8% | MSCI World Index ($Cdn.) |
| Private Real Estate Pool ($726 million) | Actively Managed Real Estate Fund | 16.7%** (gross) 12.7%** (net) | 16.1% ** (gross) | Frank Russell Commercial Property Index |

* Benchmark returns include the reinvestment of income as well as realized and unrealized capital gains.
** 1998 calendar year return.

The Global Structured Equity Pool (GSEP) and the Foreign Equity Managers Pool were the significant sources of under-performance. GSEP invested in swap agreements where counterparties agree to pay foreign index returns, on a hedged basis. Because the Canadian dollar depreciated in 1998-99, those returns were reduced compared to what they would have been unhedged. As a result, GSEP under-performed its benchmark, the MSCI World Index, which is unhedged.

The Foreign Equity Managers are external investment management firms hired to invest actively in foreign equity markets, either on a regional basis (U.S., Europe, Pacific Basin and Emerging Markets) or on a global basis. There were two factors behind their under-performance. First, a small number of large capitalized companies contributed to most of the MSCI's strong performance, making it a difficult market for active managers to out-perform. This was particularly evident in U.S.-related investment activities. Second, the foreign managers under-weighted the U.S. market, which has consistently appeared to be the most overvalued market over the last two years but which continued to be the strongest world equity market.

The Private Real Estate Pool (PREP) gross rate of return was 16.7% during the 1998 calendar year compared to the benchmark Frank Russell Commercial Property Index return of 16.1%. PREP's net rate of return, which deducts costs such as capital expenditures, leasing costs, mortgage payments, tenant improvements and administrative expenses, was 12.7%. Returns are shown for the 1998 calendar year because PREP's properties are appraised once a year.

The domestic marketable securities products met or exceeded the broad market indices against which they are measured. Falling interest rates in the latter half of 1998 created strong capital gains for the Canadian Dollar Public Debt (CDPD) Pool. The benchmark index, because of its shorter average term to maturity, did not benefit as much from falling rates. As a result, CDPD's return exceeded that of the benchmark.

Most of the Canadian Pooled Equity's (CPE) good performance occurred during the last three quarters of 1998-99. While all market participants benefited from a strong rebound in the market, the CPE also enjoyed the benefits of a more conservative portfolio, a bias towards high-growth companies, and good stock selection in the financial services sector.

## ALBERTA HERITAGE SAVINGS TRUST FUND

1998-99 marks the second full year since the Alberta Heritage Savings Trust Fund was restructured. Based on consultations with Albertans in 1994-95 and the recommendations of the March 1995 all-party report, Future Directions for Alberta's Heritage Fund, a revised Alberta Heritage Savings Trust Fund Act was passed in 1996 and came into effect in January 1997. An all-party Standing Committee of the Legislative Assembly was established to review the activities of the Fund and to approve its business plan and annual report. The committee also conducts public meetings to report on the Fund's investment activities and on the performance of the Fund.

The approved business plan for the Fund has three goals:

1. to earn income to support the government's fiscal plan,
2. to maximize long-term financial returns, and
3. to improve Albertans' understanding of the fund.

To meet these goals, two separate portfolios were established in January 1997, a Transition Portfolio and an Endowment Portfolio. The Transition Portfolio was established with assets of $10.6 billion. The Transition Portfolio is invested primarily in fixed-income securities in order to generate income to fund current government programs. At March 31, 1999, the fair market value of the assets in the Transition Portfolio was $8,205 million.

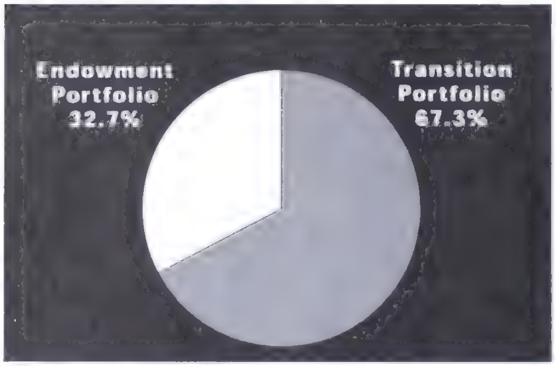
The Endowment Portfolio was established with assets of $1.2 billion. The objective of this portfolio is to maximize long-term financial returns. As a result, it has a heavier emphasis on equity investments. At a minimum, $1.2 billion is transferred from the Transition Portfolio to the Endowment Portfolio each year. By no later than 2005, all of the assets will be fully invested in the Endowment Portfolio. At March 31, 1999, the fair market value of the assets in the Endowment Portfolio was $4,334 million.

The Heritage Fund's inflation-proofing policy will change in 1999-2000. Prior to the change, the Endowment Portfolio retained a proportion of its net income each year to keep up with inflation. The remainder of the net income was transferred from the Heritage Fund to the province's General Revenue Fund. On March 23, 1999, the Fiscal Responsibility Act received Royal Assent. The Act stipulates that, until the province's accumulated debt is eliminated, the Provincial Treasurer is

not required to retain any net income for inflation proofing in the Heritage Fund, but may retain such amounts as the Provincial Treasurer considers advisable.

## Heritage Fund Performance

**HERITAGE FUND ASSETS (COST BASIS)**
**AT MARCH 31, 1999**
Total: $12,098 million




- The Fund earned net income of $932.0 million in income in 1998-99, down from $947.3 million a year earlier, reflecting lower realized capital gains due to market volatility and having a lower proportion of the assets invested in fixed income securities.
- On March 31, 1999, the total equity of the Fund was $12,026.3 million on a cost basis, unchanged from 1998. On a fair market value basis, the total equity in the fund was $12,714.2 million, down from $12,969.5 million on March 31, 1998 due to the transfer of the net income to the province's General Revenue Fund.
- Over the year, $1,205.4 million (at cost) was transferred from the Transition Portfolio to the Endowment Portfolio.
- The Transition Portfolio returned 5.4% and under-performed its benchmark of 5.9% by 50 basis points. The under-performance was due to some equity holdings that earned poor returns and to high cash holdings relative to the benchmark. $100 million in cash is required monthly in order to be transferred to the Endowment Portfolio.
- The Endowment Portfolio returned 4.7%, in line with the benchmark rate of return. The foreign equity component of the Heritage Fund under-performed its benchmark. This was offset by the better-than-benchmark performance of the Canadian equities component.
- The Endowment Portfolio rate of return exceeded that of other institutional funds. A survey reports a median return of only 1.3% for such funds for the year ending March 31, 1999.

- Combining the Transition Portfolio and the Endowment Portfolio, the Fund as a whole returned 7.5% (annualized) on average over the last two years, compared to the market cost of the Province's Canadian dollar debt of 6.8% (annualized).
- On March 31, 1999 the long-run equity benchmark exposure for the Endowment Portfolio was increased to 60% from 55% and the foreign equity benchmark exposure was increased from 20% to 30%.

Treasury released quarterly updates and the annual report on the performance of the Heritage Fund. In addition, the Standing Committee once again undertook a series of public meetings to report on the Fund and answer Albertans' questions.

### BANKING AND SECURITIES ADMINISTRATION

Treasury provides banking services to most government entities and securities administration services for Treasury's Investment Management and Liability Management divisions. Some of the major results achieved during the year included:

- Effectively and efficiently handled cash flow of $230 billion, including revenues, expenses and investment and debt transactions.
- Ensured that all surplus cash was invested on a daily basis.
- A rate of return of 5.2% was earned on the Consolidated Cash Investment Trust Fund, exceeding the performance benchmark of a 4.9% return.
- Assisted in implementation of electronic reconciliation of ministry bank accounts.
- Supported and co-ordinated the settlement of new debt issues in the amount of $2.6 billion required to refinance, in part, $3.5 billion of provincial debt that matured or was redeemed during 1998-99.

BANKING AND SECURITIES ADMINISTRATION

*Concentrate cash, settle investment and debt transactions, and make disbursements via efficient systems and banking arrangements*

### LOANS AND GUARANTEES

Loans and Guarantees administers major project loan agreements and guarantee and indemnity agreements. In addition, the division oversees the wind up of a number of provincial corporations, including N.A. Properties (1994) Ltd. (NAP) and AGT Commission, which own non-core financial assets (loans, mortgages and foreclosed real estate).

In accordance with government policy, Loans and Guarantees is disposing of remaining non-core financial assets and contingent liabilities under administration. The target is zero excluding on-going programs. The division has a target of recovering at least book value on non-core financial assets.

LOANS AND GUARANTEES

*Loan guarantees administered by Treasury down to $310 million*

Total non-core financial assets administered by the division were reduced during 1998-99 by $282 million to $313 million. Assets disposed of included the Heritage Fund loan to Al-Pac, which was sold by the province for $260 million, recovering all principal and $10 million of interest. NAP recovered about $1.7 million on its provisions for loan losses. Remaining non-core financial assets in NAP are now nominal.

Total guarantees administered by Treasury were substantially reduced by $167 million to $310 million at March 31, 1999 from $477 million at March 31, 1998.

### INVESTMENT AND DEBT ACCOUNTING

The Investment and Debt Accounting Group provides financial and performance reporting, and accounting advice and support to the Investment Management and Liability Management divisions. Some of the results of the year included timely reporting of:

- quarterly and yearly financial statements for the Alberta Heritage Savings Trust Fund, Alberta Heritage Scholarship Fund and Alberta Heritage Foundation for Medical Research Endowment Fund,
- investment information for the public sector pension plans and the long term disability funds, and
- performance of the investment and liability portfolios.

### INVESTMENT AND DEBT INFORMATION SYSTEMS

The Investment and Debt Information Systems group (IDIS) was split away from Banking and Securities Administration in April of 1998. IDIS is responsible for supporting the computerized applications that are used by Investment Management, Liability Management, Investment & Debt Accounting Group and Banking & Securities Administration to manage financial assets and liabilities on the Province's behalf. Some of the major results achieved during the year included:

- Development and implementation of an Executive Information Reporting (EIR) system. The EIR System is an online application which produces a set of Executive Management reports containing summary information about dealer activity, portfolio holdings, performance, investment exposure, trade details, and performance attribution compiled from various areas within Treasury Operations.

- Ensuring all computerized applications and systems interfaces used by Investment Management, Liability Management, Banking and Securities Administration, and Investment and Debt Accounting Group are Year 2000 ready.
- Development of a Swap database to support the administration and reporting of swap transactions negotiated on the Province's behalf.
- Re-engineering and implementation of an enhanced version of the Consolidated Cash Investment Trust Fund cash management system. The system tracks banking activity of participants' accounts, manages the allocation of daily earnings to fund participants, and provides management reports.
- Implemented an automated process for reconciling investment holdings with the Province's domestic custodians.
- Provided ongoing support for the third party securities management software used to report on the activities, status and performance of the debt and investment portfolios managed by Alberta Treasury.

GOAL 5

# AN EFFICIENT, FAIR AND COMPETITIVE CAPITAL MARKET AND AN EFFICIENT AND FAIR REGULATORY ENVIRONMENT FOR FINANCIAL INSTITUTIONS

ALBERTA SECURITIES COMMISSION

*A fair and efficient capital market in Alberta and confidence in that market*

## ALBERTA SECURITIES COMMISSION

The Alberta Securities Commission (ASC) is an industry-funded provincial corporation that regulates the capital market in Alberta and balances the interests of investors, issuers and persons registered to sell securities. The ASC administers the Securities Act, Securities Regulations and Securities Commission Rules, which promote a fair and efficient capital market in Alberta with a high level of investor confidence.

ASC regulatory functions primarily address disclosure and other market conduct issues. The Commission provides public access to certain financial and corporate information filed by issuers. It registers and monitors persons and companies trading or underwriting in securities or commodity contracts. It takes enforcement action against violators under the Securities Act and hears appeals of decisions made by the Executive Director of ASC and the Alberta Stock Exchange.

During the 1998-99 fiscal year, the ASC undertook a number of initiatives aimed at improving the efficiency of the capital market and strengthening investor confidence. This included:

- preparing the Securities Amendment Act, 1999, with a view to updating, clarifying and harmonizing Alberta securities legislation with securities legislation across Canada,
- initiating and conducting prosecutions under the Securities Act as part of a five-year pilot project between the ASC and the Minister of Justice/Attorney General of Alberta. Securities offences are now receiving a higher priority and are being prosecuted by ASC lawyers who are specialists in securities law,
- leading the development of investor education initiatives through the establishment of the independent Alberta Capital Market Foundation dedicated to providing funding for the education of investors about capital formation and funding to entrepreneurs as a means of improving the capital formation process in Alberta, and
- establishing, together with the Ontario and British Columbia Securities Commissions, the self-regulatory Mutual Fund Dealers Association which will increase protection for purchasers of mutual funds.

The Canadian Securities Administrators (CSA) consist of ten provincial and three territorial securities administrators. Together with the Canadian Council of Insurance Regulators (CCIR) and Canadian Association of Pension Supervisory Authorities (CAPSA), the CSA established the joint forum of Financial Market Regulators to address areas of common concerns to improve protection for consumers of financial products. The ASC, together with the CSA, continued to play a leadership role in the development of the Canadian Securities Regulatory System (CSRS). The CSRS includes a system of mutual reliance for the review of prospectuses and applications for exemptive relief and for the registration of Self-Regulatory Organization member securities dealers, their salespersons and advisors.

Other CSRS initiatives currently under development include:

- a national registration database that will contain information on registrants in all jurisdictions in Canada and will assist in the adoption of a system of mutual reliance for registration. The database will make it easier for persons to register while improving public access to information,
- an insider trading database that will receive insider reports in electronic and paper formats and will disseminate the information through a website, and
- an updated SEDAR (System for Electronic Document Analysis and Retrieval) that now allows listed companies to file required public information electronically with the Canadian stock exchanges.

The ASC is fully Y2K compliant and is working with other members of the CSA to try to ensure Y2K compliance of various members of the financial services industry and listed companies.

**Key Performance Measure**
**ALBERTA'S MARKET SHARE OF INVESTMENT CAPITAL**

| |
|---|
| Capital in the amount of $8.6 billion was raised through prospectus offerings, mutual funds and private placements in the province in 1998-99. This represents approximately 9.4% of the total capital raised in Canada, excluding government debt. The $8.6 billion is lower than the $9.7 billion raised in 1997-98, but Alberta's share of 9.4% is up from 8.5% in 1997-98. Treasury's target is to maintain Alberta's market share of investment capital. |

## REGULATORY ACTIVITIES

Treasury regulates the credit union, insurance, loan and trust industries in Alberta, balancing the interests of stakeholders including depositors, insurance policy holders, investors, insurance intermediaries and the companies themselves.

Regulation of these industries primarily involves disclosure and market conduct issues, and issues concerning the enforcement of legislation. Treasury provides access to financial and corporate information about credit unions and loan and trust companies through public registries.

Disclosure requirements for insurance segregated funds have been harmonized. Insurance and securities regulators are conducting a national review of the regulations surrounding segregated funds and mutual funds to ensure that the regulations are appropriate and consistent.

Treasury monitors provincially incorporated insurers and trust corporations and enforces solvency legislation. Treasury's role with respect to providing deposit insurance is restricted to ensuring that the Credit Union Deposit Guarantee Corporation is capable of fulfilling its guarantee of credit union deposits. All provincially incorporated trust and insurance companies met the solvency requirements and no financial failures were recorded for loan or trust companies or credit unions in 1998-1999.

Changes to the legislation governing the credit union system were proclaimed in order to support a level playing field with other financial institutions and to simplify its regulatory process. Treasury also oversaw the drafting of a new Insurance Act that is required to address modernization concerns of the financial services industry and its stakeholders. The legislation was passed in the Spring 1999 session of the Legislative Assembly and is expected to be proclaimed into force early next year. Some of the significant changes include:

- provincial insurers will be incorporated by letters patent under the Insurance Act,
- mandatory errors and omissions insurance for agents and adjusters,
- mandatory continuing education for agents and adjusters,
- regulating the sale of credit-related insurance by financial institutions and car dealers, and
- broader enforcement powers and higher penalties.

Treasury received feedback from Alberta incorporated credit unions, insurers, loan and trust companies, and Credit Union Central, Alberta to determine if they had complied with directives and recommendations related to legislation and sound business practices. Treasury's target of 100% compliance was achieved. The feedback also indicated that companies were making good progress on implementing optional recommendations relating to operating matters.

A survey was conducted of financial institutions that verified more than 80% were satisfied or very satisfied with the efficiency and fairness of the regulatory environment, meeting the target set out in Treasury's business plan.

### CREDIT UNION DEPOSIT GUARANTEE CORPORATION

The Credit Union Deposit Guarantee Corporation (CUDGC) regulates the solvency of credit unions in Alberta and is responsible for ensuring that all credit unions operate in compliance with the Credit Union Act.

CREDIT UNION DEPOSIT GUARANTEE CORPORATION

*Encourage sound business practices of the Alberta Credit Unions and guarantee the repayment of all deposits according to legislation*

The primary role of the Corporation is to guarantee deposit protection to deposit holders with credit unions in Alberta. CUDGC also assists, advises and, on occasion, directs credit unions to ensure that sound business practices are maintained. The Corporation monitors and regulates credit union performance by conducting examinations and working closely with credit unions on improving the regulatory environment of the system. It also provides loan review and approval for certain credit union loans. During 1998, the Corporation issued six lending bulletins to credit unions and reduced the length of loan approval replies.

It is important that all credit unions meet the legislated capital adequacy requirements by October 31, 1999. For 1998, the overall consolidated capital of all credit unions met the requirement while the number of individual credit unions meeting the capital adequacy levels increased to 83% (81% in 1997). CUDGC projects that 95% of credit unions will meet these capital requirements by the end of 1999.

The credit-union-funded Deposit Guarantee Fund managed by CUDGC exceeded the 1.0% minimum target for equity in the Fund, achieving an equity level of 1.15% of total credit union assets. The growth in the equity level helped the Corporation to reduce the assessment rate charged to credit unions to 0.17% (from 0.18%). CUDGC also administers the Master Bond Fund that provides insurance coverage for credit unions and maintained a $2.3 million fund equity.

The Corporation consulted with credit union representatives and distributed a new set of Lending Guidelines to credit unions in 1998. Capital adequacy and the credit union's management of Y2K plans are high priorities for 1999.

## ALBERTA INSURANCE COUNCIL AND AUTOMOBILE INSURANCE BOARD

ALBERTA INSURANCE COUNCIL

*To ensure a fair and efficient marketplace for the distribution of insurance products*

The Alberta Insurance Council (AIC) is responsible for conducting examinations, licensing, regulating and disciplining of insurance agents, brokers, and adjusters in Alberta and for investigating consumer complaints against the industry.

During 1998, AIC co-ordinated the submissions of the Life, General, and Insurance Adjusters Council to the Alberta Government relating to the new Insurance Act. In 1999, AIC will be assisting the Treasury department in developing new regulations and revising existing regulations before the Act is proclaimed.

AIC is involved, along with other provincial regulators, in a comprehensive study of life insurance agent education with the objective of ensuring that agents have a level of technical knowledge sufficient to maintain a high standard of consumer protection.

The Automobile Insurance Board reviews and approves the insurers' rating programs for compulsory auto coverage and investigates matters respecting automobile insurance premiums in Alberta.

Premiums for third party liability continue to increase in response to the persistent rise in frequency and severity of bodily injury claims. Collision and comprehensive coverage have yielded satisfactory results, partially offsetting the less favourable results for third party liability.

The Board endorses initiatives to improve traffic safety records such as "Think and Drive" that are aimed at reducing accidents through driver awareness campaigns.

GOAL 6

# QUALITY FINANCIAL SERVICES TO ALBERTANS THROUGH ALBERTA TREASURY BRANCHES, ALBERTA MUNICIPAL FINANCING CORPORATION AND ALBERTA PENSIONS ADMINISTRATION CORPORATION

## ALBERTA TREASURY BRANCHES (ATB)

ATB's Here Today . . . Here Tomorrow business plan identified three corporate strategies which support ATB's objective of being Albertans' financial services provider of choice in independent business, agri-industry and individual financial services. These strategies are: (1) focus on core target markets - independent business, agri-industry and individual financial services, (2) increase profitability, and (3) get the best value for every dollar spent. Particular initiatives completed during the fiscal year included:

- increased retail deposits by $252 million in a highly competitive market,
- increased ATB's mortgage portfolio by nearly 16%,
- installed 44 new Automated Banking Machines, broadening customer access,
- increased the competencies of ATB staff - nearly 3,000 full and part-time employees attended training programs this year, and
- substantially improved productivity ratios.

During 1998-99, significant progress was made in the following areas supporting ATB's business strategies:

- creating a Corporate Learning Centre to ensure that ATB employees are given the training and tools to excel in their jobs. In the first six months of operations, over 5,000 days of training were provided,
- initiating information technology business strategies focusing on Year 2000 compliance and the installation of a standardized software and hardware structure throughout the organization, and
- establishing a sales support centre to centralize mortgage administration, freeing staff to deliver products and services to ATB customers.

Other highlights during the fiscal year included the outsourcing of information technology and document processing to IBM-ISM and Intria, respectively. These arrangements give ATB access to leading edge technologies without the capital investment otherwise required. In April 1998, a new compensation plan was introduced which links

ALBERTA TREASURY BRANCHES

*Ready for Tomorrow – Focus on Markets, People and Service.*

performance and pay more closely. This plan is similar to those existing in the financial services sector, linking remuneration to performance. During the year, the branch service delivery system was realigned based on a relationship management model. Relationship managers in the larger urban centres are responsible for offering specialized financial services and unbiased advice to independent and commercial business and to agri-industry clients.

### Financial Results

ATB's estimate for net income during the year was $46 million. Actual profit was greater than estimated at $111 million (see table below). The main reasons for the improvement were continued low loan loss provisions, continuing strong net interest margins of 3.2% and the increase in average performing assets. All financial targets were exceeded with the exception of Other Income, and growth targets for loans, deposits and assets. In March 1999, for the first time since 1985, ATB had a positive year-end equity position in excess of $44 million. This achievement of eliminating the ATB's accumulated deficit comes one year ahead of plan.

**ALBERTA TREASURY BRANCHES FINANCIAL RESULTS**
as at March 31 (percentage)

| | 1999 Actual | 1999 Target | Industry Comparison* | 1998 Actual |
|---|---|---|---|---|
| Operating revenue growth | 14.0 | 2.5 | 8.2 | 3.5 |
| Net interest margin | 3.2 | 2.8 | 1.8 | 2.9 |
| Net interest spread on average earning assets | 3.2 | 2.8 | 2.1 | 3.0 |
| Other income to operating income | 20.5 | 24.7 | 45.1 | 20.7 |
| Expenses to operating revenue | 68.3 | 77.0 | 67.8 | 74.3 |
| Return on assets (before tax) | 1.2 | 0.5 | 0.9 | 1.0 |
| Loan Growth | 7.7 | 7.9 | 8.9 | 2.2 |
| Deposit Growth | 3.4 | 6.2 | 9.1 | 3.8 |
| Asset Growth | 5.3 | 7.4 | 13.2 | 4.2 |
| Credit Losses to Total Loans | 0.1 | 0.4 | 0.3 | (0.1) |

* ***Source:*** Average of seven major Canadian banks - DBRS Annual Review of Canadian Banking Sector, for the year ended October 31, 1998.

The industry comparison for operating revenue growth includes growth from acquisitions and such items as capital market activities and investment management fees resulting from trading, investment banking and brokerage activities. ATB has no equivalent for these activities. This observation also applies to the industry comparison of other income to operating income.

**$ IN MILLIONS AS AT MARCH 31**

| | 1999 Actual | 1999 Target | 1998 Actual |
|---|---|---|---|
| Net interest income | 286.9 | 244.3 | 251.2 |
| Other income | 74.1 | 80.2 | 65.5 |
| Non-interest expense | 246.6 | 250.0 | 235.3 |
| Net income | 110.7 | 46.3 | 85.4 |

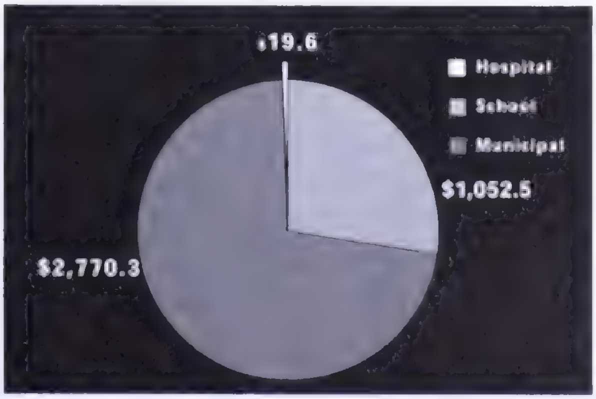
## ALBERTA MUNICIPAL FINANCING CORPORATION

Alberta Municipal Financing Corporation (AMFC) provides local authorities within the province with funding for capital projects at the lowest possible cost, consistent with the viability of the Corporation. Today, AMFC provides financing for 14 cities, two specialized municipalities, 228 towns and villages, 36 counties, 30 municipal and improvements districts, 18 irrigation and water services commissions, 28 health authorities, 70 school districts/divisions, three universities and seven colleges.

AMFC offers a range of borrowing terms to its shareholders at rates comparable to the province's borrowing costs. The Corporation's goals are to provide local authorities with funding at the lowest possible cost and to maintain the lowest administrative and new loan costs compared to other municipal borrowing corporations. AMFC continues to have the lowest new issue and ongoing administration costs per $1,000 of loans of similar organizations in Canada.

The AMFC has taken a number of deliberate steps over the past decade in order to reduce the level of the Corporation's surplus. The Corporation has reduced interest rates from highs of over 17% to 12%, issued interest rebates of $113 million, allowed a limited prepayment policy at a reduced penalty instead of full cost, and has established an interest rate policy which allows the Corporation's shareholders to borrow at a rate similar to the Province's borrowing cost. The accumulated effect of these steps has and will impact the Corporation's income into the future. The Corporation recorded a loss of $14.9 million in 1998 and is projecting losses of $38.1 and $48.3 million in 1999 and 2000 respectively, and then a small profit in 2001. These projections are of course subject to the Corporation's loan activity but the Board of Directors believes that these projected losses will not reduce the viability nor the creditworthiness of the Corporation.

**ALBERTA MUNICIPAL FINANCING CORPORATION**
Loans Outstanding by Purpose as at December 31, 1998
($ millions)



*Visit APA's website at www.apaco.ab.ca*

## ALBERTA PENSIONS ADMINISTRATION CORPORATION

Alberta Pensions Administration Corporation (APA) became a provincial Crown corporation in 1996. It is responsible for administering eight pension plans under the direction of five pension boards and the Government of Alberta. Services are provided to approximately 500 employers, 47,000 pensioners and 142,000 members, including 22,000 deferred members. The combined assets of the pension plans exceeded $15 billion at December 31, 1998. The Investment Management Division of Alberta Treasury administers these assets.

APA's business is to collect pension contributions, maintain members' accounts, pay pension benefits and provide information to pension boards, employers, members and pensioners. In 1998, APA focused on three major initiatives aimed at improving the effectiveness and efficiency of its business:

- The Business Process Re-Engineering project was initiated to streamline APA's business practices and improve computer systems to serve customers better. New pension software (PENFAX) was selected and information technology services were outsourced to SHL Systemhouse.
- Communications capabilities were improved by replacing approximately 110 desktop computers, installing e-mail and developing and installing a corporate web site that enables direct access to information by our customers. Also, APA provided 100 member information sessions, 81 employer workshops and 793 one-on-one counseling sessions.
- In November 1998, the Corporation commenced restructuring by transferring about 80 staff from the Treasury department to APA. Mission and vision statements were created for the Corporation. Employee skills were enhanced by providing training and a skills inventory was developed to target skill requirements.

APA met its performance targets as set out in Treasury's 1998-99 business plan. A survey conducted by Quantitative Services Measurement (QSM) confirmed that APA had the lowest per member administrative costs in 1998 compared to other Canadian public sector pension plan survey participants that had fewer than 300,000 members. APA's average per member administrative cost was $62 in 1998, based on QSM's survey methodology. In addition, the 1998 customer survey conducted by the Corporation verified that 83% of the 220 employers who responded are satisfied or very satisfied with APA's services.

Despite increased workload in 1998, the Corporation continued to improve its delivery of pension administration services. APA will continue to improve its products and services in the coming year.

In 1999, APA will commence installing new pension software and will migrate data for each pension plan member from legacy systems to a new client server for the Special Forces and Local Authorities Pension Plans. This new software is expected to further improve customer satisfaction with service processes and system operations. The Corporation will also develop new performance management and recognition programs for its employees.

## PERFORMANCE MEASURES IN THE 1998-99 TO 2000-01 BUSINESS PLAN NOT REPORTED IN THE 1998-99 ANNUAL REPORT

| Goal | Performance Measure | Reason for not Reporting |
|---|---|---|
| 2 | • Satisfaction of Albertans that the government's financial and performance report is complete and accurate; target: four out of five Albertans satisfied or very satisfied.<br>• Portion of Albertans aware of the government's budget situation in the coming year; target: four out of five Albertans aware. | • Survey of Albertans did not include these two questions as the question on Albertans' awareness of the government's financial performance was considered adequate. |
| 3 | • Voluntary compliance rate with tax programs; target: 97% | • The performance measure methodology was developed and piloted in 1998-99. The objective is to implement the methodology across all tax programs in 1999-2000. |
| 5 | • Satisfaction of consumers and insurance intermediaries with the quality of assistance, advice and and information provided; target: four out of five satisfied or very satisfied. | • Survey was not undertaken. Form and frequency of survey is under review. |

# TREASURY FINANCIAL STATEMENTS

# Treasury Financial Statements

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CONSOLIDATED FINANCIAL STATEMENTS
MARCH 31, 1999

## AUDITOR'S REPORT

To the Members of the Legislative Assembly

I have audited the consolidated statement of financial position of the Ministry of Treasury as at March 31, 1999 and the consolidated statements of operations and changes in financial position for the year then ended. These financial statements are the responsibility of the management of the Ministry. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

The Ministry of Treasury is required to follow the corporate government accounting policies and reporting practices as disclosed in Note 3. These accounting policies have been established by Alberta Treasury and are consistent across ministries. With certain exceptions, the basis of accounting is in accordance with generally accepted accounting principles. My reservation of opinion in this auditor's report identifies an exception from generally accepted accounting principles that arises from following the accounting policies established by Alberta Treasury.

The accounting policy for pension obligations is an exception from generally accepted accounting principles. Obligations to pension plans for current and former employees of all other departments have been recognized as a liability in the accompanying statement of financial position and consequently the annual change in the liability for all departments has been recognized in the statement of operations. In my view, on a basis of allocation similar to that used for Provincial agencies, an amount of approximately $52 million due to pension plans, in the other departments' capacity as employer at March 31, 1999, should not be recognized as a liability in these financial statements. The effect of this overstatement of liabilities is to understate expenses for the year ended March 31, 1999 by $19 million.

In my opinion, except for the effects of the matter discussed in the preceding paragraph, these consolidated financial statements present fairly, in all material respects, the financial position of the Ministry as at March 31, 1999 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles.

Peter Valentine, FCA
Auditor General

Edmonton, Alberta
May 21, 1999

## MINISTRY OF TREASURY
## CONSOLIDATED STATEMENT OF OPERATIONS
## FOR THE YEAR ENDED MARCH 31, 1999

| | In thousands | | |
|---|---|---|---|
| | 1999 | | 1998 |
| | Budget (Schedule 2) | Actual | Actual |
| **Revenues** (Schedules 1 and 2): | | | |
| Income taxes | $ 5,313,106 | $ 6,259,679 | $ 5,725,099 |
| Other taxes | 1,107,362 | 1,065,858 | 1,088,269 |
| Non-renewable resource revenue: | | | |
| Royalty tax credit | (233,000) | (249,486) | (225,406) |
| Transfers from Government of Canada | 3,931 | 3,692 | 3,931 |
| Investment income | 1,453,231 | 1,627,819 | 1,785,233 |
| Net income from commercial operations | 50,073 | 124,376 | 96,201 |
| Fees, permits and licences | 11,159 | 13,766 | 13,698 |
| Other | 24,511 | 32,500 | 30,316 |
| | 7,730,373 | 8,878,204 | 8,517,341 |
| **Expenses** (Schedules 2 and 3) | | | |
| Ministry support services | 4,970 | 5,753 | 4,724 |
| Revenue collection and rebates | 13,502 | 12,293 | 12,125 |
| Financial management and planning | 23,441 | 25,177 | 43,798 |
| Pensions administration | 10,753 | 11,163 | 9,302 |
| Regulation of securities markets | 7,927 | 10,223 | 7,349 |
| Regulation of the insurance industry | 1,480 | 1,429 | 1,305 |
| Transfers to the Alberta Heritage Foundation for Medical Research | 36,000 | 36,000 | 32,000 |
| Transfers to the Students Finance Board for payment of Alberta Heritage Scholarships | 13,000 | 12,480 | 11,939 |
| Corporate tax interest refunds | 13,000 | 98,253 | 18,206 |
| Farm credit stability and small business term assistance programs | 6,500 | 6,913 | 10,145 |
| Pension liability funding | 92,000 | 70,676 | 90,165 |
| Valuation adjustments (Schedule 4) | (67,000) | (52,305) | (127,636) |
| Debt servicing costs: | | | |
| Provincial purposes | 1,084,000 | 1,257,301 | 1,174,041 |
| Municipal, hospital and school purposes | 483,827 | 462,802 | 503,025 |
| | 1,723,400 | 1,958,158 | 1,790,488 |
| **Net operating results** | $ 6,006,973 | $ 6,920,046 | $ 6,726,853 |

The accompanying notes and schedules are part of these financial statements.

MINISTRY OF TREASURY
CONSOLIDATED STATEMENT OF FINANCIAL POSITION
MARCH 31, 1999

| | In thousands | |
|---|---|---|
| | 1999 | 1998 |
| **Assets:** | | |
| Cash | $ 358,175 | $ 326,320 |
| Accrued interest and accounts receivable (Schedule 5) | 1,093,942 | 1,058,390 |
| Portfolio investments (Schedule 6) | 12,121,276 | 11,270,926 |
| Equity in commercial enterprises (Schedule 7) | 195,952 | 64,962 |
| Loans and advances to government entities (Schedule 8) | 1,436,143 | 1,772,736 |
| Other loans and advances (Schedule 9) | 4,082,718 | 4,847,082 |
| Inventories held for resale | 72 | 58 |
| Capital assets (Schedule 10) | 7,339 | 5,846 |
| | $19,295,617 | $19,346,320 |
| **Liabilities:** | | |
| Accrued interest and accounts payable (Schedule 11) | $ 644,253 | $ 741,667 |
| Unmatured debt (Schedule 12) | 12,979,233 | 13,160,921 |
| Debt of Alberta Municipal Financing Corporation (Schedule 13) | 3,788,001 | 4,028,195 |
| Pension obligations (Schedule 14) | 1,027,274 | 1,082,181 |
| Other accrued liabilities (Schedule 15) | 117,901 | 140,952 |
| Equity in Alberta Municipal Financing Corporation (Schedule 13) | 307,516 | 330,583 |
| | 18,864,178 | 19,484,499 |
| **Net Assets (Liabilities):** | | |
| Net assets (liabilities) at beginning of year | (138,179) | (2,822,494) |
| Net operating results | 6,920,046 | 6,726,853 |
| Net transfer to general revenues | (6,350,428) | (4,042,538) |
| Net assets (liabilities) at end of year | 431,439 | (138,179) |
| | $19,295,617 | $19,346,320 |

The accompanying notes and schedules are part of these financial statements.

## MINISTRY OF TREASURY
## CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION
## FOR THE YEAR ENDED MARCH 31, 1999

| | In thousands | |
|---|---|---|
| | 1999 | 1998 |
| **Operating transactions:** | | |
| Net operating results | $ 6,920,046 | $ 6,726,853 |
| Non-cash items included in net operating results | (12,913) | (75,460) |
| | 6,907,133 | 6,651,393 |
| Change in equity in Alberta Municipal Financing Corporation | (23,067) | 16,118 |
| Other, net | (137,231) | 32,061 |
| Cash provided by operating transactions | 6,746,835 | 6,699,572 |
| **Investing transactions:** | | |
| Proceeds from disposals, repayments and redemptions of portfolio investments | 7,664,589 | 12,996,342 |
| Repayment of loans and advances | 1,701,970 | 2,060,336 |
| Portfolio investments | (7,594,002) | (14,088,733) |
| Loans and advances | (1,309,508) | (1,249,450) |
| Other, net | (38,793) | 23,737 |
| Cash provided by (used for) investing transactions | 424,256 | (257,768) |
| **Financing transactions:** | | |
| Debt issues | 23,970,385 | 13,697,278 |
| Debt retirement | (24,759,193) | (16,173,889) |
| Net transfer to general revenues | (6,350,428) | (4,042,538) |
| Cash used for financing transactions | (7,139,236) | (6,519,149) |
| **Net cash provided (used)** | 31,855 | (77,345) |
| **Cash at beginning of year** | 326,320 | 403,665 |
| **Cash at end of year** | $ 358,175 | $ 326,320 |

The accompanying notes and schedules are part of these financial statements.

MINISTRY OF TREASURY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEAR ENDED MARCH 31, 1999

Note 1 Authority

The Provincial Treasurer has been designated as responsible for various Acts by the Government Organization Act and its regulations. To fulfil these responsibilities, the Provincial Treasurer administers the organizations listed below. The authority under which each organization operates is also listed. Together, these organizations form the Ministry of Treasury (the Ministry).

| Organization | Authority |
|---|---|
| Department of Treasury (the Department) | Government Organization Act, Statutes of Alberta 1994, as amended |
| Alberta Heritage Foundation for Medical Research Endowment Fund | Alberta Heritage Foundation for Medical Research Act, Chapter A-26, Revised Statutes of Alberta 1980, as amended |
| Alberta Heritage Savings Trust Fund | Alberta Heritage Savings Trust Fund Act, Chapter A-27.01, Statutes of Alberta 1996 |
| Alberta Heritage Scholarship Fund | Alberta Heritage Scholarship Act, Chapter A-27.1, Statutes of Alberta 1981, as amended |
| Alberta Risk Management Fund | Financial Administration Act, Revised Statutes of Alberta 1980, as amended |
| Utility Companies Income Tax Rebates Fund | Utility Companies Income Tax Rebates Act, Chapter U-10, Revised Statutes of Alberta 1980, as amended |
| Alberta Insurance Council | Insurance Act, Chapter I-5, Revised Statutes of Alberta 1980, as amended |
| Alberta Municipal Financing Corporation | Alberta Municipal Financing Corporation Act, Chapter A-33, Revised Statutes of Alberta 1980, as amended |
| Alberta Pensions Administration Corporation | Incorporated August 10, 1995 under the Business Corporations Act, Chapter B-15, Statutes of Alberta 1981, as amended |
| Alberta Securities Commission | Incorporated June 1, 1995 under the Securities Act, Chapter S-6.1, Statutes of Alberta 1981, as amended |
| The Alberta Government Telephones Commission and its subsidiaries | Telecommunications Act, Chapter T-3.5, Statutes of Alberta 1988, as amended, and the Alberta Government Telephones Reorganization Act, Chapter A-23.5, Statutes of Alberta 1990 |
| Alberta Treasury Branches and its subsidiary | Alberta Treasury Branches Act, Chapter A-37.9, Statutes of Alberta 1997 |
| Credit Union Deposit Guarantee Corporation | Credit Union Act, Chapter C-31.1, Statutes of Alberta 1989, as amended |
| N.A. Properties (1994) Ltd. | Amalgamated corporation under the Business Corporations Act, Chapter B-15, Statutes of Alberta 1981, as amended |
| S C Financial Ltd. | Incorporated May 29, 1986 under the Business Corporations Act, Chapter B-15, Statutes of Alberta 1981, as amended, as a wholly owned company of the Credit Union Deposit Guarantee Corporation |
| Chembiomed Ltd. | Incorporated under the Canada Business Corporations Act |
| Gainers Inc. and its subsidiaries | Incorporated under the Business Corporations Act, Chapter B-15, Statutes of Alberta 1981, as amended |

Note 2 Purpose

The Ministry's core functions are to:

(a) Provide analysis and recommendations to the Provincial Treasurer and Treasury Board;

(b) Maintain a framework that fosters government accountability;

(c) Administer and collect tax revenue;

(d) Manage the province's financial assets and liabilities;

(e) Foster a fair and efficient financial marketplace; and

(f) Provide financial services through Alberta Treasury Branches, Alberta Municipal Financing Corporation, and Alberta Pensions Administration Corporation.

Note 3 Summary of Significant Accounting Policies and Reporting Practices

The recommendations of the Public Sector Accounting Board of the Canadian Institute of Chartered Accountants are the primary source for the disclosed basis of accounting. Recommendations of the Accounting Standards Board of the Canadian Institute of Chartered Accountants, other authoritative pronouncements, accounting literature, and published financial statements relating to either the public sector or analogous situations in the private sector are used to supplement the recommendations of the Public Sector Accounting Board where it is considered appropriate.

These financial statements are prepared in accordance with the following accounting policies.

**(a) Method of Consolidation**

The accounts of the Department, the Alberta Heritage Foundation for Medical Research Endowment Fund, the Alberta Heritage Savings Trust Fund, the Alberta Heritage Scholarship Fund, the Alberta Risk Management Fund, the Utility Companies Income Tax Rebates Fund, Alberta Insurance Council, Alberta Municipal Financing Corporation, Alberta Pensions Administration Corporation, and Alberta Securities Commission are consolidated after adjusting them to a basis consistent with the accounting policies described below in (b). Intra-ministry transactions (revenues, expenses, investing and financing transactions, and related asset and liability accounts) have been eliminated.

The accounts of Provincial agencies and other entities designated as commercial enterprises (the Alberta Government Telephones Commission and its subsidiaries, Alberta Treasury Branches and its subsidiary, Credit Union Deposit Guarantee Corporation, N.A. Properties (1994) Ltd., and S.C. Financial Ltd.), and commercial Crown-controlled corporations (Chembiomed Ltd. and Gainers Inc. and its subsidiaries) are reported on an equity basis, the equity being computed in accordance with generally accepted accounting principles.

The reporting period of some of the Provincial agencies is other than March 31. Transactions of these agencies that have occurred during the period to March 31, 1999 and that significantly affect the consolidation have been recorded.

**(b) Basis of Financial Reporting**

**Revenues**

All revenues are reported on the accrual method of accounting. Corporate income tax receipts in abeyance are recorded as accounts payable.

**Expenses**

Expenses represent the cost of resources consumed during the year on Ministry operations. Expenses include amortization of capital assets.

Pension costs included in these statements comprise the cost of employer contributions for current service of employees during the year and additional government and employer contributions for employees' service relating to prior years.

Certain expenses, primarily for office space and legal advice, incurred on behalf of the Ministry by other Ministries are not reflected in the consolidated statement of operations.

**Valuation Adjustments**

Valuation adjustments include changes in the valuation allowances used to reflect financial assets at their net recoverable or other appropriate value. Valuation adjustments also represent the change in management's estimate of future payments arising from obligations relating to guarantees, indemnities, pension obligations, and accrued employee vacation entitlements.

Valuation adjustments for pension obligations include interest on the Ministry's share of the unfunded liability, the amortization of deferred adjustments over the expected average remaining service life of employees, and the effect of the change in the ratio used to allocate a plan's total unfunded liability to participating entities.

**Assets**

Financial assets are limited to financial claims on outside organizations and individuals and inventories held for resale at the year end.

Portfolio investments are carried at cost. Realized gains and losses on disposals of these investments are included in the determination of net operating results for the year. Where there has been a loss in value of an investment that is other than a temporary decline, the investment is written down to recognize the loss. The written down value is deemed to be the new cost.

Loans are recorded at cost less any unearned income and allowance for credit loss. Discounts recorded as the result of interest rate reductions given on loans to local authorities are amortized to investment income over the term of the loans. Where there is no longer reasonable assurance of timely collection of the full amount of principal and interest of a loan, a provision for credit loss is made and the carrying amount of the loan is reduced to its estimated realizable amount.

Inventories for resale are valued at the lower of cost, determined on a first-in, first-out basis, and estimated net realizable value.

Capital assets of the Ministry are recorded at historical cost and amortized on a straight line basis over the estimated useful lives of the assets. Assets acquired by right are not included. In addition, donated capital assets are recorded at nil cost.

**Liabilities**

Liabilities include all financial claims payable by the Ministry at the year end.

Debentures included in unmatured debt are recorded at the face amount of the issue less unamortized discount, which includes issue expenses and hedging costs.

Income or expense on interest rate swaps and forward interest rate agreements used to manage interest rate exposure is recorded as an adjustment to debt servicing costs. The exchange gain or loss on the foreign exchange contracts used to manage currency exposure is deferred and amortized over the life of the contract.

Certain liabilities, such as pension obligations, are reflected in these financial statements on behalf of all departments.

**Foreign Currency**

Foreign currency transactions are translated into Canadian dollars using average rates of exchange, except for hedged foreign currency transactions which are translated at rates of exchange established by the terms of the forward exchange contracts. Exchange differences on unhedged transactions are included in the determination of net operating results for the year.

**Measurement Uncertainty**

Estimates are used in accruing revenues and expenses in circumstances where the actual accrued revenues and expenses are unknown at the time the financial statements are prepared. Uncertainty in the determination of the amount at which an item is recognized in financial statements is known as measurement uncertainty. Such uncertainty exists when there is a variance between the recognized amount and another reasonably possible amount, as there is whenever estimates are used.

Measurement uncertainty that is material to these financial statements exists in the accrual of personal and corporate income taxes, provisions for pensions and loans and advances. The nature of the uncertainty in these items arises from several factors such as the effect on accrued taxes of the verification of taxable income; the effect on accrued pension obligations of actual experience compared to assumptions; and the effect on loans and advances of actual collectibility and changes in economic conditions. While best estimates have been used for reporting items subject to measurement uncertainty, management considers that it is possible, based on existing knowledge, that changes in future conditions in the near term could require a material change in the recognized amounts. Near term is defined as a period of time not to exceed one year from the date of the financial statements.

**(c) Change in Accounting Policy**

Pension expense associated with the Teachers' Pension Plan that was previously reported in the consolidated financial statements of the Ministry of Treasury on behalf of the Ministry of Education is now reported by the Ministry of Education. Net operating results increased by $42,509,000 (1998 $199,107,000) as a result of this change.

The Ministry no longer reports liabilities associated with Teachers' Pension Plan entitlements. These liabilities are now reported in the consolidated financial statements of the Ministry of Education. Pension obligations and net liabilities have decreased by $3,783,184,000 (1998 $3,804,500,000) as a result of this change.

This change has been applied retroactively and prior periods have been restated to reflect the change.

Note 4 Restricted Assets

Financial assets include $204,124,000 (1998 $187,499,000) of sinking fund investments which are restricted for the settlement of debt issues of Alberta Municipal Financing Corporation.

Note 5 Risk Management

**(a) Liability Management**

The objective of the Ministry's liability management program is to achieve the lowest cost on debt within an acceptable degree of variability of debt servicing costs. In order to achieve this objective, the Ministry manages four risks - interest rate risk, currency exchange risk, credit risk, and refunding risk. The Ministry manages these four risks within approved policy guidelines. The management of these risks and the policy guidelines apply to the Ministry's unmatured debt, excluding debt raised to fund requirements of provincial corporations and regulated funds. Debt of provincial corporations and regulated funds is managed separately in relation to their assets.

The policy guideline for interest rate risk is that Canadian dollar floating rate debt should be between 38 per cent and 50 per cent of total Canadian dollar debt. The policy guideline for currency exchange risk is that there be no exposure to currencies other than United States dollars. Further, the unhedged U.S. dollar debt should not exceed US$3,000,000,000.

Credit risk relating to swaps is minimal as management deals only with the most credit worthy counterparties. The policy guideline for refunding risk is that term debt maturities should not exceed $3,500,000,000 in any fiscal year, excluding early redemption of Alberta Capital Bonds and Alberta Savings Certificates.

These policies were complied with during the year.

**(b) Asset Management**

The majority of the Ministry's portfolio investments are in the Alberta Heritage Savings Trust Fund (Heritage Fund).

The Heritage Fund is comprised of two portfolios. The Endowment Portfolio has the objective of maximizing long-term financial returns. The portfolio is comprised of 35 per cent to 55 per cent fixed income instruments and 45 per cent to 65 per cent equities. The Transition Portfolio has the objective of providing income support to the government's fiscal plan over the short term to medium term. The portfolio consists mainly of Canadian fixed income securities.

The investments in the Alberta Heritage Foundation for Medical Research Endowment Fund and the Alberta Heritage Scholarship Fund are managed to preserve the capital of the funds over time and to provide an annual level of income for grants. Alberta Municipal Financing Corporation's sinking fund is managed to repay maturing debt of the corporation.

Note 6 Commitments and Contingencies

Set out below are details of commitments to organizations outside the Ministry and contingencies resulting from guarantees, indemnities and litigation, other than those reported as liabilities and shown in Schedule 15.

Management considers that the contingencies will not result in any material adverse effect on the Ministry. Any losses arising from the settlement of contingencies are treated as current year expenses.

### (a) Commitments

Commitments to outside organizations in respect of contracts entered into before March 31, 1999 amounted to $116,635,000 (1998 $102,682,000). These commitments will become expenses of the Ministry when terms of the contracts are met. These amounts include obligations under operating leases which expire on various dates to March 31, 2005. The aggregate amounts payable for the unexpired terms of these leases are as follows:

| | |
|---|---|
| 1999-2000 | $18,498,000 |
| 2000-01 | $15,835,000 |
| 2001-02 | $13,639,000 |
| 2002-03 | $11,655,000 |
| 2003-04 | $ 9,543,000 |

### (b) Guarantees

Guarantees at March 31, 1999 amounting to $304,040,000 (1998 $468,646,000) are analyzed in Schedule 16. This schedule is included with the financial statements because payments under guarantees are a statutory charge on the Ministry.

### (c) Contingencies of Commercial Enterprises

The Credit Union Deposit Guarantee Corporation has a potential liability under guarantees relating to deposits of credit unions. At December 31, 1998 credit unions in Alberta held deposits totalling $4,771,124,000 (1997 $4,424,265,000), and had assets in excess of deposits.

At March 31, 1999, Alberta Treasury Branches had a potential liability under guarantees and letters of credit amounting to $424,346,000 (1998 $411,813,000). During the year, Alberta Treasury Branches initiated legal actions which resulted in counterclaims aggregating $475,500,000. The eventual outcome of these claims and counterclaims is not determinable.

N.A. Properties (1994) Ltd. has provided guarantees of principal and interest on mortgages sold to Canadian Western Bank. The principal and interest on these mortgages totalled $32,882,000 at March 31, 1999 (1998 $48,082,000).

### (d) Legal Actions

At March 31, 1999, the Ministry was named as defendant in various legal actions, including legal actions relating to insurance claims. The total claimed in specific legal actions amounts to approximately $146,201,000 (1998 $161,237,000).

The resulting loss, if any, from these claims cannot be determined.

## Note 7 Valuation of Financial Assets and Liabilities

Fair value is the amount of consideration agreed upon in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act.

The fair values of cash, accrued interest, receivables and payables, are estimated to approximate their book values

The methods used to determine the fair values of portfolio investments are explained in the following paragraphs.

Public fixed-income securities and equities are valued at the year-end closing sale price, or the average of the latest bid and ask prices quoted by an independent securities valuation company.

Mortgages and certain non-public provincial debentures are valued based on the net present value of future cash flows. These cash flows are discounted using appropriate interest rate premiums over similar Government of Canada benchmark bonds trading in the market.

The fair value of private equities is estimated by management.

Real estate investments are reported at their most recent appraised value, net of any liabilities against the real property. Real estate properties are appraised annually by qualified external real estate appraisers.

Fair values of loans and advances are not reported due to there being no organized financial market for the instruments and it is not practicable within constraints of timeliness or cost to estimate the fair values with sufficient reliability.

The fair value of unmatured debt and debt held by Alberta Municipal Financing Corporation is an approximation of its fair value to the holder.

At the year end, the fair value of investments and any other assets and liabilities denominated in a foreign currency are translated at the year end exchange rate.

### Note 8 Related Party Transactions

The Ministry is responsible for handling cash transactions of all departments and their funds. As a result, the Ministry engages in transactions with all other ministries in the normal course of operations.

During the 1998-99 fiscal year, the Ministry, on behalf of the Department of Education, paid $107,647,000 (1998 $186,836,000) to repay Ministry loans. This amount was accounted for as part of net transfer to general revenues.

Net transfer to general revenues also includes amounts provided to Agriculture Financial Services Corporation, Alberta Opportunity Company and Alberta Social Housing Corporation by the responsible departments and to the Department of Education to enable them to pay interest on Ministry loans. The interest, amounting to $232,105,000 for the year ended March 31, 1999 (1998 $293,799,000), is included in investment income.

The Controller, a senior official of the Ministry, was a director of PSC Payment Systems Corporation (PSC) which, until March 31, 1999, was 40 per cent owned by the Government of Alberta, through the Ministry. The Controller did not receive any benefit during the year, in cash or in kind, as a result of this directorship. The investment in and transactions with PSC were not significant to the Ministry, on both a cost and equity basis.

Accommodations, legal, telecommunications and personnel services were provided to the Ministry during the year by other ministries at no cost.

The Ministry and its employees paid certain taxes and fees set by regulation for permits, licences, and other rights. These amounts were incurred in the normal course of business and reflect charges applicable to all users.

### Note 9 Trust Funds Under Administration

The Ministry administers trust funds that are regulated funds consisting of public money over which the Legislature has no power of appropriation. Because the Ministry has no equity in the funds and administers them for the purposes of various trusts, they are not included in the Ministry's consolidated financial statements.

As at March 31, 1999, trust funds under administration were as follows:

| | In thousands | |
|---|---|---|
| | 1999 | 1998 |
| Local Authorities Pension Plan Fund | $ 7,771,333 | $ 7,571,914 |
| Public Service Pension Plan Fund | 3,674,083 | 3,579,475 |
| The Workers' Compensation Board Accident Fund | 2,703,227 | 2,909,897 |
| Universities Academic Pension Plan Fund | 1,566,196 | 1,562,932 |
| Management Employees Pension Plan Fund | 1,334,290 | 1,279,737 |
| Special Forces Pension Plan Fund | 856,245 | 841,281 |
| Regional Health Authorities and various health institutions construction accounts | 164,866 | 103,297 |
| Other | 76,048 | 275,148 |
| | $ 18,146,288 | $ 18,123,681 |

### Note 10 Uncertainty Due to the Year 2000

The year 2000 issue is the result of some computer systems using two digits rather than four to define the applicable year. Government computer systems that have date sensitive software may recognize a date using "00" as the year 1900 rather than the year 2000, which could result in miscalculations or system failures. In addition, similar problems may arise in some systems if certain dates in 1999 are not recognized as a valid date or are recognized to represent something other than a date. The effects of the year 2000 issue may be experienced before, on, or after January 1, 2000. If not addressed, the effect on operations and financial reporting may range from minor errors to significant systems failure that could affect the ability to conduct some government operations. Despite the government's efforts to address this issue, it is not possible to be certain that all aspects of the year 2000 issue affecting the government, including those related to the efforts of customers, suppliers and other third parties, will be fully resolved.

Note 11 Comparative Figures

Certain 1998 figures have been reclassified to conform to the 1999 presentation.

Due from general revenues reported in 1998 has been reclassified to net liabilities in 1999. The change in net liabilities reported on the statement of financial position includes the transfer to general revenues. As a result, the net contribution to general revenues as previously reported is no longer required.

Note 12 Approval of Financial Statements

These financial statements were approved by the Acting Corporate Secretary and the Deputy Provincial Treasurer.

MINISTRY OF TREASURY
SCHEDULES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEAR ENDED MARCH 31, 1999

Schedule 1

REVENUES

| | In thousands | | |
|---|---|---|---|
| | 1999 | | 1998 |
| | Budget | Actual | Actual |
| Income taxes: | | | |
| Personal income tax | $ 3,835,048 | $ 4,600,762 | $ 3,876,571 |
| Corporate income tax | 1,642,287 | 1,658,917 | 1,848,528 |
| Corporate income tax cushion | (164,229) | - | - |
| | 5,313,106 | 6,259,679 | 5,725,099 |
| Other taxes: | | | |
| Fuel tax | 570,000 | 546,918 | 557,980 |
| Tobacco tax | 345,000 | 341,333 | 329,919 |
| Insurance corporations tax | 112,047 | 101,555 | 121,532 |
| Hotel room tax | 41,000 | 44,614 | 42,371 |
| Financial institutions capital tax | 39,315 | 31,438 | 36,467 |
| | 1,107,362 | 1,065,858 | 1,088,269 |
| Non-renewable resource revenue: | | | |
| Royalty tax credit | (233,000) | (249,486) | (225,406) |
| Transfers from Government of Canada: | | | |
| Unconditional subsidy | 3,931 | 3,692 | 3,931 |
| Investment income | 1,453,231 | 1,627,819 | 1,785,233 |
| Net income from commercial operations: | | | |
| Alberta Treasury Branches | 46,338 | 110,692 | 85,434 |
| Other | 3,735 | 13,684 | 10,767 |
| | 50,073 | 124,376 | 96,201 |
| Fees, permits and licences: | | | |
| Alberta Securities Commission | 9,614 | 11,482 | 10,704 |
| Insurance companies, agents and brokers | 800 | 1,700 | 1,763 |
| Other | 745 | 584 | 1,231 |
| | 11,159 | 13,766 | 13,698 |
| Other: | | | |
| Sale of assets | 2,000 | - | - |
| Refunds of expenditure | 588 | 3,913 | 1,153 |
| Miscellaneous | 21,923 | 28,587 | 29,163 |
| | 24,511 | 32,500 | 30,316 |
| | $ 7,730,373 | $ 8,878,204 | $ 8,517,341 |

## BUDGET

In thousands

For the year ended March 31 1999

| | 1998-99 Estimates (a) | Adjustments and Reallocations (b) | 1998-99 Budget | Voted Supplementary (a) | 1998-99 Authorized Budget |
|---|---|---|---|---|---|
| **Revenues** | | | | | |
| Income taxes | $ 5,313,106 | $ - | $ 5,313,106 | $ - | $ 5,313,106 |
| Other taxes | 1,107,362 | - | 1,107,362 | - | 1,107,362 |
| Non-renewable resource revenue | | | | | |
| Royalty tax credit | (233,000) | - | (233,000) | - | (233,000) |
| Transfers from Government of Canada | 3,931 | - | 3,931 | - | 3,931 |
| Investment income | 1,453,231 | - | 1,453,231 | - | 1,453,231 |
| Net income from commercial operations | 50,073 | - | 50,073 | - | 50,073 |
| Fees, permits and licences | 11,159 | - | 11,159 | - | 11,159 |
| Other | 24,511 | - | 24,511 | 1,182 | 25,693 |
| | 7,730,373 | - | 7,730,373 | 1,182 | 7,731,555 |
| **Expenses** | | | | | |
| Ministry support services | 4,970 | - | 4,970 | 775 | 5,745 |
| Revenue collection and rebates | 13,502 | - | 13,502 | | 13,502 |
| Financial management and planning | 23,441 | - | 23,441 | 1,182 | 24,623 |
| Pensions administration | 10,753 | - | 10,753 | - | 10,753 |
| Regulation of securities markets | 7,927 | - | 7,927 | - | 7,927 |
| Regulation of the insurance industry | 1,480 | - | 1,480 | - | 1,480 |
| Transfers to the Alberta Heritage Foundation for Medical Research | 36,000 | - | 36,000 | - | 36,000 |
| Transfers to the Students Finance Board for payment of Alberta Heritage Scholarships | 13,000 | - | 13,000 | - | 13,000 |
| Corporate tax interest refunds | 13,000 | - | 13,000 | | 13,000 |
| Farm credit stability and small business term assistance programs | 6,500 | - | 6,500 | - | 6,500 |
| Pension liability funding | 155,500 | (63,500) | 92,000 | - | 92,000 |
| Valuation adjustments | 30,000 | (97,000) | (67,000) | - | (67,000) |
| Debt servicing costs: | | | | | |
| Provincial purposes | 1,084,000 | - | 1,084,000 | - | 1,084,000 |
| Municipal, hospital and school purposes | 483,827 | - | 483,827 | - | 483,827 |
| | 1,883,900 | (160,500) | 1,723,400 | 1,957 | 1,725,357 |
| **Net operating results** | $ 5,846,473 | $ 160,500 | $ 6,006,973 | $ (775) | $ 6,006,198 |

(a) Government estimates were approved on March 26, 1998 and Supplementary Estimates were approved on March 8, 1999.

(b) Adjustments and reallocations consist of: $(63,500,000) of pension liability funding for the Teachers' Pension Plan transferred to the Ministry of Education as a result of the change in accounting policy referred to in Note 3(c); $76,000,000 for pension provisions referred to in Budget '98 but not included in the Estimates; and $(173,000,000) for pension provisions relating to the Teachers' Pension Plan transferred to the Ministry of Education as a result of the change in accounting policy referred to in Note 3(c).

Schedule 3

EXPENSES BY OBJECT

| | 1999 Budget | 1999 Actual | 1998 Actual |
|---|---|---|---|
| | In thousands | | |
| Salaries, wages and employee benefits | $ 33,372 | $ 35,922 | $ 33,134 |
| Supplies and services | 25,564 | 24,459 | 42,261 |
| Grants | 49,000 | 49,647 | 43,938 |
| Interest and amortization of unrealized exchange gains and losses | 1,567,542 | 1,720,077 | 1,677,014 |
| Pension liability funding | 92,000 | 70,676 | 90,165 |
| Corporate tax interest refunds | 13,000 | 98,253 | 18,206 |
| Other financial transactions | 8,036 | 8,736 | 11,810 |
| Amortization of capital assets | 1,886 | 2,693 | 1,596 |
| Valuation adjustments | (67,000) | (52,305) | (127,636) |
| | $ 1,723,400 | $ 1,958,158 | $ 1,790,488 |

Schedule 4

VALUATION ADJUSTMENTS

| | 1999 Budget | 1999 Actual | 1998 Actual |
|---|---|---|---|
| | In thousands | | |
| Provision for doubtful accounts and loans | $ 15,000 | $ 10,260 | $ 117,037 |
| Provision for guarantees and indemnities | 15,000 | (8,429) | (17,287) |
| Provision for employee benefits other than pensions | - | 776 | 9,318 |
| Provision for settlement with Principal Group noteholders | - | - | (15,000) |
| Pension provisions | (97,000) | (54,912) | (221,704) |
| | $ (67,000) | $ (52,305) | $ (127,636) |

Schedule 5

ACCRUED INTEREST AND ACCOUNTS RECEIVABLE

| | 1999 | 1998 |
|---|---|---|
| | In thousands | |
| Personal income tax | $ 462,467 | $ 330,748 |
| Accrued interest receivable | 339,453 | 401,481 |
| Corporate income tax | 206,633 | 209,713 |
| Fuel tax | 45,242 | 48,813 |
| Insurance corporations tax | 24,669 | 36,618 |
| Financial institutions capital tax | 7,998 | 13,144 |
| Tobacco tax | 3,540 | 3,584 |
| Forward contracts | - | 3,467 |
| Other | 8,142 | 14,966 |
| | 1,098,144 | 1,062,534 |
| Less: Allowance for doubtful accounts | 4,202 | 4,144 |
| | $ 1,093,942 | $ 1,058,390 |

## PORTFOLIO INVESTMENTS

| | In thousands | | | |
|---|---|---|---|---|
| | 1999 | | 1998 | |
| | Book Value | Fair Value | Book Value | Fair Value |
| Fixed-income securities (a)(b): | | | | |
| Government of Canada, direct and guaranteed | $ 2,444,591 | $ 2,480,976 | $ 2,976,647 | $ 3,097,862 |
| Provincial, direct and guaranteed | 1,873,591 | 1,916,251 | 2,181,732 | 2,282,591 |
| Municipal | 71,888 | 75,165 | 66,265 | 69,758 |
| Corporate | 2,859,156 | 2,894,541 | 2,980,229 | 3,021,568 |
| Pooled investment funds | 2,280,389 | 2,264,678 | 1,457,046 | 1,465,353 |
| | 9,529,615 | 9,631,611 | 9,661,919 | 9,937,132 |
| Equities (b): | | | | |
| Canadian | 911,227 | 1,370,758 | 696,514 | 1,344,947 |
| Foreign | 1,490,381 | 1,592,820 | 877,563 | 947,640 |
| Real estate | 190,053 | 198,521 | 34,930 | 39,234 |
| | 2,591,661 | 3,162,099 | 1,609,007 | 2,331,821 |
| | $ 12,121,276 | $ 12,793,710 | $ 11,270,926 | $ 12,268,953 |

(a) The majority of the Ministry's fixed-income securities are in the Transition Portfolio of the Alberta Heritage Savings Trust Fund. As at March 31, 1999, the Transition Portfolio held $6,931,516,000 (1998 $7,363,321,000) of public fixed-income securities at cost (Fair value $7,043,987,000 (1998 $7,562,574,000)). The securities held have an average effective yield of 4.91% per annum (1998 4.84% per annum) based on market for securities maturing in a year, and 5.30% per annum (1998 5.34% per annum) for securities maturing between 1 and 35 years. As at March 31, 1999, the Portfolio has the following term structure based on par:

| | 1999 | | 1998 |
|---|---|---|---|
| | | % | |
| Under 1 year | 10 | | 13 |
| 1 to 5 years | 56 | | 55 |
| 6 to 10 years | 33 | | 31 |
| Over 10 years | 1 | | 1 |

(b) The Alberta Heritage Savings Trust Fund uses index swaps and interest rate swaps to enhance return and for hedging risks. As at March 31, 1999, the notional amount of index swaps and interest rate swaps issued by the Heritage Fund amounted to $1,528,823,000 (1998 $880,961,000).

Schedule 7

EQUITY IN COMMERCIAL ENTERPRISES

| | In thousands | |
|---|---|---|
| | 1999 | 1998 |
| **Accumulated surpluses (deficits):** | | |
| Accumulated surpluses (deficits) at beginning of year | $ (8,126) | $ (122,517) |
| Total revenue | 758,743 | 704,061 |
| Total expenditure | 632,759 | 588,213 |
| Net revenue | 125,984 | 115,848 |
| Net transfers to departments | (10,090) | (1,457) |
| Accumulated surpluses (deficits) at end of year | $ 107,768 | $ (8,126) |
| **Represented by:** | | |
| Assets: | | |
| Loans | $ 8,037,266 | $ 7,462,293 |
| Investments (a) | 200,000 | 400,000 |
| Other assets | 1,440,743 | 1,541,381 |
| Total assets | 9,678,009 | 9,403,674 |
| Liabilities: | | |
| Accounts payable | 347,931 | 285,735 |
| Deposits | 9,022,310 | 8,726,065 |
| Unmatured debt | 200,000 | 400,000 |
| Total liabilities | 9,570,241 | 9,411,800 |
| | $ 107,768 | $ (8,126) |
| **Accumulated surpluses (deficits) at end of year:** | | |
| Credit Union Deposit Guarantee Corporation | $ 62,471 | $ 58,702 |
| Alberta Treasury Branches | 44,148 | (66,544) |
| The Alberta Government Telephones Commission | 1,035 | 947 |
| N.A. Properties (1994) Ltd. | 114 | (1,231) |
| | 107,768 | (8,126) |
| **Elimination of inter fund agency balances** | 88,184 | 73,088 |
| **Equity in commercial enterprises at end of year** | $ 195,952 | $ 64,962 |

(a) Investments include $194,000,000 (1998 $192,000,000) of sinking fund notes which are restricted for the settlement of debt issues of The Alberta Government Telephones Commission.

Schedule 8

## LOANS AND ADVANCES TO GOVERNMENT ENTITIES

| | In thousands | |
|---|---|---|
| | 1999 | 1998 |
| Alberta Social Housing Corporation | $ 662,781 | $ 932,825 |
| Agriculture Financial Services Corporation | 647,391 | 635,017 |
| Alberta Opportunity Company | 85,747 | 77,100 |
| Environmental Protection and Enhancement Fund | 40,000 | - |
| Public Trustee | 224 | 224 |
| Alberta School Foundation Fund | - | 73,000 |
| Advances to revolving funds | - | 54,570 |
| | $ 1,436,143 | $ 1,772,736 |

Schedule 9

## OTHER LOANS AND ADVANCES

| | In thousands | |
|---|---|---|
| | 1999 | 1998 |
| Alberta Municipal Financing Corporation Act (a) | $ 3,668,560 | $ 3,990,739 |
| Farm Credit Stability Act | 290,269 | 425,230 |
| Alberta Heritage Savings Trust Fund Act | 149,836 | 562,226 |
| Centennial Food Corporation | 13,850 | 14,250 |
| Pratt & Whitney Canada Ltd. | 4,187 | 4,465 |
| Board of Governors of the University of Alberta | 3,218 | 3,474 |
| Accountable advances | 1,392 | 1,357 |
| University of Lethbridge Students' Union | 1,362 | 1,480 |
| University of Calgary Students' Union | 1,249 | 1,506 |
| Advances under the Municipal Land Loans Act | 1,070 | 2,025 |
| Implemented guarantees and indemnities | 438 | 488 |
| Judgement debts | 286 | 420 |
| University of Alberta Students' Union | 233 | 455 |
| Loans to municipalities | 155 | 299 |
| Small Business Term Assistance Act | 4 | 486 |
| Canadian Western Bank | - | 4 |
| Other | 186 | 186 |
| | 4,136,295 | 5,009,090 |
| Less: Allowance for doubtful loans, advances, implemented guarantees and indemnities | 53,577 | 162,008 |
| | $ 4,082,718 | $ 4,847,082 |

(a) Municipal loans on average yield 10.1% per annum (1998 10.9%) and have the following term structure as at March 31, 1999

| | 1999 | 1998 |
|---|---|---|
| | % | |
| Under 1 year | 1 | 2 |
| 1 to 5 years | 24 | 15 |
| 6 to 10 years | 42 | 37 |
| Over 10 years | 33 | 46 |

Schedule 10

## CAPITAL ASSETS

| | Estimated Useful Life | 1999 Cost | 1999 Accumulated Amortization | 1999 Net Book Value | 1998 Net Book Value |
|---|---|---|---|---|---|
| | | In thousands | | | |
| Equipment | 10 years | $ 2,362 | $ 664 | $ 1,698 | $ 2,226 |
| Computer hardware and software | 5 years | 23,437 | 18,315 | 5,122 | 3,085 |
| Other | 10 years | 623 | 104 | 519 | 535 |
| | | $ 26,422 | $ 19,083 | $ 7,339 | $ 5,846 |

Schedule 11

## ACCRUED INTEREST AND ACCOUNTS PAYABLE

| | 1999 | 1998 |
|---|---|---|
| | In thousands | |
| Accrued interest on unmatured debt and debt of Alberta Municipal Financing Corporation | $ 505,424 | $ 509,141 |
| Corporate income tax receipts in abeyance | 103,105 | 86,026 |
| Investment purchases | 2,977 | 84,601 |
| Alberta Social Housing Corporation | 2,338 | 2,572 |
| Unearned revenue | 1,858 | 2,699 |
| Other | 28,551 | 56,628 |
| | $ 644,253 | $ 741,667 |

UNMATURED DEBT

Schedule 12

| | | | In thousands | | | |
|---|---|---|---|---|---|---|
| | 1999 | | | | 1998 | |
| | Effective Rate (a)(b)(c) | Modified Duration (d) | Book Value (a) | Fair Value (a) | Book Value (a) | Fair Value (a) |
| | % | years | | | | |
| Canadian dollar debt and fully hedged foreign currency debt: | | | | | | |
| Floating rate and short-term fixed rate debt (e) | 6.05 | 0.29 | $ 3,510,354 | $ 3,555,000 | $ 3,042,136 | $ 3,096,000 |
| Fixed rate long-term debt (f) | 7.34 | 4.86 | 5,221,545 | 5,976,000 | 5,585,433 | 6,416,000 |
| | 6.82 | 3.16 | 8,731,899 | 9,531,000 | 8,627,569 | 9,512,000 |
| Unhedged U.S. dollar debt (g): | | | | | | |
| Floating rate and short-term fixed rate debt (e) | 4.90 | 0.16 | 2,363,715 | 2,469,000 | 3,046,178 | 3,224,000 |
| Fixed rate long-term debt | 7.37 | 1.99 | 1,883,619 | 2,105,000 | 1,487,174 | 1,682,000 |
| | 6.02 | 1.00 | 4,247,334 | 4,574,000 | 4,533,352 | 4,906,000 |
| Total unmatured debt | 6.56 | 2.46 | $ 12,979,233 | $ 14,105,000 | $ 13,160,921 | $ 14,418,000 |

(a) Book value represents the amount the Ministry owes. Fair value is an approximation of market value to the holder. The book value, fair value and weighted average effective rate include the effect of interest rate and currency rate swaps. For non-marketable issues, the effective rate and fair value are determined by reference to yield curves for comparable quoted issues.

(b) Weighted average effective rates on unhedged U.S. dollar debt are based upon debt stated in U.S. dollars.

(c) Weighted average effective rate on total unmatured debt is on debt inclusive of deferred exchange losses on unhedged U.S. dollar debt (see note (g)).

(d) Modified duration is the weighted average term to maturity of the security's cash flows (i.e., interest and principal) and is a measure of price volatility; the greater the modified duration of a bond, the greater its percentage price volatility.

(e) Floating rate debt includes short-term debt, term debt with less than one year remaining to maturity, and term debt with interest rate reset within a year.

(f) Canadian dollar fixed rate debt includes $678,696,000 (1998 $678,696,000) held by the Canada Pension Plan Investment Fund.

(g) Unhedged U.S. dollar debt is translated into Canadian dollars at the March 31 noon exchange rate of $1.5092 per U.S. dollar (1998 $1.4166 per U.S. dollar). Deferred exchange losses on unhedged U.S. dollar debt amounted to $149,000,000 at March 31, 1999 (1998 $168,000,000). Amortization of deferred exchange losses amounted to $302,000,000 for the year ended March 31, 1999 (1998 $154,000,000).

Debt principal repayment requirements at par in each of the next five years, including short-term debt maturing in 1999-2000, and thereafter are as follows:

| | | |
|---|---|---|
| 1999-2000 | $2,479,000,000 | (includes U.S. $403,000,000 unhedged) |
| 2000-01 | $2,194,000,000 | (includes U.S. $800,000,000 unhedged) |
| 2001-02 | $1,397,000,000 | (includes U.S. $356,000,000 unhedged) |
| 2002-03 | $ 855,000,000 | (includes U.S. $500,000,000 unhedged) |
| 2003-04 | $1,745,000,000 | (includes U.S. $500,000,000 unhedged) |
| Thereafter | $3,755,000,000 | (includes U.S. $362,000,000 unhedged) |

Some of the debt has call provisions. Years to maturity reflect original maturity date and not early call date. Debt with call provisions occurring in under one year is $450,000,000, and in one to five years is $285,000,000.

UNMATURED DEBT (continued)

**Derivative financial instruments**

The Ministry uses interest rate swaps and currency rate swaps and contracts to manage the interest rate risk and currency exposure associated with unmatured debt. In addition, forward interest rate agreements are used to manage interest rate exposure in the short term. Associated with these instruments are credit risks that could expose the Ministry to potential losses. Credit risk relates to the possibility that a loss may occur from the failure of another party to perform according to the terms of a contract. Credit exposure to counterparties is a fraction of the notional principal amount, as shown in the table below. The Ministry minimizes its credit risk associated with these contracts by dealing with only the most credit worthy counterparties.

Interest rate swaps involve the exchange of a series of interest payments, either at a fixed or floating rate, based upon a contractual or notional principal amount. An interest rate swap agreement based upon a notional amount involves no exchange of underlying principal. The notional amount serves as the basis for determining the exchange of interest payments. At March 31, 1999, interest rate swap agreements were being used primarily to convert fixed interest rate payments to floating rates.

Cross currency interest rate swaps involve both the swapping of interest rates and currencies.

Currency rate swaps including foreign exchange contracts involve an agreement to exchange United States dollars and other currencies into Canadian and United States dollars at an agreed upon rate and on an agreed settlement date.

The following table summarizes the Ministry's derivative portfolio and related credit exposure:

**Notional amount:** represents the amount to which a rate or price is applied in order to calculate the exchange of cash flows.

**Replacement cost:** represents the cost of replacing, at current market rates, all contracts which have a positive market value.

| | In thousands | | | |
|---|---|---|---|---|
| | 1999 | | 1998 | |
| | Notional Amount | Replacement Cost | Notional Amount | Replacement Cost |
| Interest rate swaps | $ 3,175,000 | $ 263,000 | $ 2,089,000 | $ 182,000 |
| Cross currency interest rate swaps | 1,037,000 | 41,000 | 1,233,000 | 31,000 |
| Currency rate swaps including foreign exchange contracts (stated in Canadian dollars) | - | - | 31,000 | 4,000 |
| | $ 4,212,000 | $ 304,000 | $ 3,353,000 | $ 217,000 |

# Schedule 13

## DEBT OF AND EQUITY IN ALBERTA MUNICIPAL FINANCING CORPORATION

| | In thousands | |
|---|---|---|
| | 1999 | 1998 |
| Alberta Municipal Financing Corporation | | |
| Canadian dollar fixed rate debt (a) | $ 3,788,001 | $ 4,028,195 |
| Equity (b) | $ 307,516 | $ 330,583 |

(a) Canadian dollar fixed rate debt includes $3,316,761,000 (1998 $3,493,406,000) held by the Canada Pension Plan Investment Fund and has the following characteristics as at March 31, 1999 (see Schedule 12 note (a) and note (d)).

| | 1999 | 1998 |
|---|---|---|
| Fair value | $5,286,000,000 | $5,578,000,000 |
| Effective rate | 12.0% per annum | 11.4% per annum |

Debt principal repayment requirements in each of the next five years, including short-term debt maturing in 1999-2000, are as follows:

| | |
|---|---|
| 1999-2000 | $294,206,000 |
| 2000-01 | $442,367,000 |
| 2001-02 | $331,739,000 |
| 2002-03 | $724,735,000 |
| 2003-04 | $441,023,000 |

(b) Alberta Municipal Financing Corporation equity has been included in liabilities of the Ministry because it represents profits of the corporation which the corporation has the power to pay to municipal and other shareholders that have borrowed money from the corporation.

# Schedule 14

## PENSION OBLIGATIONS

Pension obligations are based upon actuarial valuations performed at least triennially using the projected benefit method prorated on services. The assumptions used in the valuations were adopted after consultation between the pension plan boards, the government and the actuaries, depending on the plan, and represent best estimates of future events. Each plan's future experience will inevitably vary, perhaps significantly, from the assumptions. Any differences between the actuarial assumptions and future experience will emerge as gains or losses in future valuations. Gains and losses are amortized over the expected average remaining service lives of the related employee groups.

The valuations were based upon economic assumptions, including a long-term rate of return on pension plan fund assets of 4.0 per cent over the level of price inflation for all the plans. The rate was based upon a long-term rate of return of 8 per cent and 4 per cent respectively for the Universities Academic and Special Forces plans, and 7.5 per cent and 3.5 per cent respectively for the Public Service Management (Closed Membership), Public Service, Management Employees and Local Authorities plans. Demographic assumptions used in the valuations reflect the experience of the plans.

The latest actuarial valuations were performed as at December 31, 1997 for the Public Service, Members of the Legislative Assembly, Management Employees and Local Authorities plans, as at December 31, 1996 for the Public Service Management (Closed Membership) and Universities plans, and as at December 31, 1995 for the Special Forces plan. Except for the Local Authorities plan, these actuarial valuations indicated a deficiency of net assets over actuarial present value of accrued benefits. Including deferred adjustments, unfunded liabilities were extrapolated to March 31, 1999.

A separate pension plan fund is maintained for each pension plan except for the Members of the Legislative Assembly plan. Pension plan fund assets are invested in both marketable investments of organizations external to the government and in Province of Alberta bonds and promissory notes.

Schedule 14 (continued)

PENSION OBLIGATIONS (continued)

| | In thousands | |
|---|---|---|
| | 1999 | 1998 |
| Obligations to pension plans for current and former employees and Members of the Legislative Assembly: | | |
| Public Service Management (Closed Membership) Pension Plan (a) | $ 656,698 | $ 656,890 |
| Public Service Pension Plan (a) | 175,920 | 189,441 |
| Members of the Legislative Assembly Pension Plan (b) | 49,119 | 57,754 |
| Management Employees Pension Plan (a) | 31,107 | 48,855 |
| | 912,844 | 952,940 |
| Obligations to pension plans for employees of organizations outside the government reporting entity: | | |
| Universities Academic Pension Plan (c) | 106,041 | 101,499 |
| Special Forces Pension Plan (c) | 8,389 | 16,683 |
| Local Authorities Pension Plan (c) | - | 11,059 |
| | 114,430 | 129,241 |
| | $ 1,027,274 | $ 1,082,181 |

(a) The Province administers three defined benefit pension plans for substantially all of its employees. The three plans are the Public Service Management (Closed Membership), the Public Service and the Management Employees pension plans. An employee can be a member of only one plan at a time.

The Public Service Management (Closed Membership) pension plan provides benefits to former members of the Public Service Management pension plan who were retired, were entitled to receive a deferred pension or had attained 35 years of service before August 1, 1992. After all assets in the plan are exhausted, all benefits under the plan will be paid by the Department.

For Public Service, the unfunded liability for service credited prior to January 1, 1992 is being financed by additional contributions in the ratio of 62.5 per cent by the Department and 18.75 per cent each by employers and employees, over the period ending on or before December 31, 2036. Current service costs are funded by employers and employees.

For Management Employees, the unfunded liability for service credited prior to January 1, 1992 is being financed by additional contributions of 0.75 per cent for employees and such percentages by employers as will be required to eliminate the unfunded liability over the period ending on or before December 31, 2043. Current service costs are funded by employers and employees.

(b) The Ministry has a liability for payment of pension benefits under a defined benefit pension plan for Members of the Legislative Assembly. Active participation in this plan was terminated as of June 1993, and no benefits can be earned for service after this date. The December 31, 1997 actuarial valuation used a discount rate of 7.5 per cent and a long term inflation rate of 3.5 per cent.

(c) Under the Public Sector Pension Plans Act, the Ministry has or previously had obligations for payment of additional contributions under defined benefit pension plans for employees of post-secondary educational institutions and local authorities. The three plans are the Universities Academic, Special Forces and Local Authorities pension plans.

For Universities Academic, the unfunded liability for service credited prior to January 1, 1992 is being financed by additional contributions of 1.25 per cent of pensionable salaries by the Ministry, and such percentages by employers and employees as will fund equally the remaining amount as determined by the plan valuation, over the period ending on or before December 31, 2043. Current service costs are funded by employers and employees.

For Special Forces, the unfunded liability for service credited prior to January 1, 1992 is being financed by additional contributions in the ratio of 45.45 per cent by the Ministry and 27.27 per cent each by employers and employees, over the period ending on or before December 31, 2036. Current service costs are funded by employers and employees. The Act provides that payment of all benefits arising from pensionable service prior to 1994, excluding post-1991 cost of living adjustment benefits, is guaranteed by the Province.

For Local Authorities, the December 31, 1997 actuarial valuation disclosed an actuarial surplus for service credited prior to January 1, 1992. Accordingly, additional contributions by the Province ceased effective January 1, 1998. The obligation reported at March 31, 1998 was eliminated during 1998-99. Current service costs are funded by employers and employees.

Schedule 15

OTHER ACCRUED LIABILITIES

| | In thousands | |
|---|---|---|
| | 1999 | 1998 |
| Guarantees and indemnities: | | |
| Credit union assistance (a) | $ 98,994 | $ 113,486 |
| Guarantees (Schedule 16) | 6,324 | 8,054 |
| Other | 3,879 | 11,682 |
| | 109,197 | 133,222 |
| Settlement with Principal Group noteholders | 5,000 | 5,000 |
| Vacation entitlements | 3,704 | 2,730 |
| | $ 117,901 | $ 140,952 |

(a) The Ministry has agreed to indemnify and fund interest to the extent necessary on $335,000,000 of debentures issued by S C Financial Ltd. to credit unions in exchange for stabilization preferred shares of the credit unions. The indemnity will expire on October 31, 2010.

Schedule 16

GUARANTEES (a)

| | In thousands | | Expiry |
|---|---|---|---|
| | 1999 | 1998 | Date |
| Farm Credit Stability Act (b) | $ 297,552 | $ 450,470 | 2011 |
| Rural utilities loans | 4,397 | 4,578 | Ongoing |
| Centre for Frontier Engineering Research | 3,055 | 3,380 | 2005 |
| Securities Act | 2,160 | - | Ongoing |
| University of Calgary | 1,357 | 1,406 | 2016 |
| Banff Centre for Continuing Education | 1,055 | 1,121 | 2014 |
| Small Business Term Assistance Act | 412 | 662 | (c) |
| Export program | 228 | 230 | (c) |
| Canadian Airlines International Ltd. | - | 11,267 | (c) |
| Pocaterra Development Corporation | - | 1,967 | (c) |
| North Saskatchewan River Boat Ltd. | - | 1,499 | (c) |
| Other under $250,000 | 148 | 120 | (c) |
| | 310,364 | 476,700 | |
| Less: Estimated liability (Schedule 15) | 6,324 | 8,054 | |
| | $ 304,040 | $ 468,646 | |

(a) Authorized loan guarantee limits decline as guaranteed loans are repaid.

The lender takes appropriate security prior to issuing a loan to the borrower which is guaranteed by the Province. The security taken depends on the nature of the loan. Interest rates are negotiated with the lender by the borrower and typically range from prime to prime plus two per cent.

No new program guarantees are being issued under the following Acts or programs: Farm Credit Stability Act, Small Business Term Assistance Act, and Export program. The guarantee program under the Rural Utilities Act is ongoing. The guarantee under the Securities Act has no expiry date.

(b) The expiry date shown is the latest expiry date for guaranteed loans under the program.

(c) Loans have expired, are in the process of realization of security, or guarantees are paid out.

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## AUDITOR'S REPORT

To the Provincial Treasurer

I have audited the statement of financial position of the Department of Treasury as at March 31, 1999 and the statements of operations and changes in financial position for the year then ended. These financial statements are the responsibility of the management of the Department. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

The Department of Treasury is required to follow the corporate government accounting policies and reporting practices as disclosed in Note 3. These accounting policies have been established by Alberta Treasury and are consistent across ministries. With certain exceptions, the basis of accounting is in accordance with generally accepted accounting principles. My reservation of opinion in this auditor's report identifies an exception from generally accepted accounting principles that arises from following the accounting policies established by Alberta Treasury.

The accounting policy for pension obligations is an exception from generally accepted accounting principles. Obligations to pension plans for current and former employees of all other departments have been recognized as a liability in the accompanying statement of financial position and consequently the annual change in the liability for all departments has been recognized in the statement of operations. In my view, on a basis of allocation similar to that used for Provincial agencies, an amount of approximately $52 million due to pension plans, in the other departments' capacity as employer at March 31, 1999, should not be recognized as a liability in these financial statements. The effect of this overstatement of liabilities is to understate expenses for the year ended March 31, 1999 by $19 million.

In my opinion, except for the effects of the matter discussed in the preceding paragraph, these financial statements present fairly, in all material respects, the financial position of the Department as at March 31, 1999 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles.

Peter Valentine, FCA
Auditor General

Edmonton, Alberta
May 21, 1999

DEPARTMENT OF TREASURY
STATEMENT OF OPERATIONS
FOR THE YEAR ENDED MARCH 31, 1999

| | In thousands | | |
|---|---|---|---|
| | 1999 | | 1998 |
| | Budget (Schedule 3) | Actual | Actual |
| **Revenues** (Schedules 1 and 2) | | | |
| Internal government transfers | $ 716,200 | $ 932,013 | $ 922,346 |
| Income taxes | 5,313,106 | 6,259,679 | 5,725,099 |
| Other taxes | 1,107,362 | 1,065,858 | 1,088,269 |
| Non-renewable resource revenue: | | | |
| Royalty tax credit | (233,000) | (249,486) | (225,406) |
| Transfers from Government of Canada | 3,931 | 3,692 | 3,931 |
| Investment income | 92,158 | 65,225 | 85,106 |
| Fees, permits and licences | 2,004 | 838 | 1,936 |
| Transfers from government enterprises | 900 | 10,137 | 9,348 |
| Other | 9,162 | 16,614 | 8,871 |
| | 7,011,823 | 8,104,570 | 7,619,500 |
| **Expenses** (Schedules 2, 3, 4 and 5) | | | |
| Voted: | | | |
| Ministry support services | 4,970 | 5,781 | 4,724 |
| Revenue collection and rebates | 13,502 | 13,055 | 12,246 |
| Financial management and planning | 17,685 | 19,277 | 27,853 |
| | 36,157 | 38,113 | 44,823 |
| Statutory: | | | |
| Corporate tax interest refunds | 13,000 | 98,253 | 18,206 |
| Farm credit stability program | 6,500 | 6,904 | 10,129 |
| Small business term assistance program | - | 9 | 16 |
| Pension liability funding | 92,000 | 70,741 | 90,218 |
| Debt servicing costs | 1,094,000 | 1,264,427 | 1,186,183 |
| | 1,205,500 | 1,440,334 | 1,304,752 |
| Valuation adjustments (Schedule 6) | (67,000) | (53,836) | (240,898) |
| | 1,174,657 | 1,424,611 | 1,108,677 |
| **Net operating results** | $ 5,837,166 | $ 6,679,959 | $ 6,510,823 |

The accompanying notes and schedules are part of these financial statements.

DEPARTMENT OF TREASURY
STATEMENT OF CHANGES IN FINANCIAL POSITION
FOR THE YEAR ENDED MARCH 31, 1999

| | In thousands 1999 | 1998 |
|---|---|---|
| **Operating transactions** | | |
| Net operating results | $ 6,679,959 | $ 6,510,823 |
| Non-cash items included in net operating results: | | |
| Amortization on investments and debt, net | | |
| Purchase and issue discounts | 68,779 | 32,210 |
| Foreign exchange losses | 307,822 | 163,171 |
| Net income on investments valued at equity | (1,343) | (3,304) |
| Amortization of capital assets | 840 | 470 |
| Valuation adjustments | (53,836) | (240,898) |
| | 7,002,221 | 6,462,472 |
| Decrease (increase) in receivables | 19,148 | (134,987) |
| Decrease in payables, including pension obligations | (24,362) | (106,811) |
| Cash provided by operating transactions | 6,997,007 | 6,220,674 |
| **Investing transactions** | | |
| Loans and advances: | | |
| Government entities | (1,165,412) | (1,092,422) |
| Other | (10,022) | (8,842) |
| Repayments of loans and advances: | | |
| Government entities | 1,064,030 | 590,341 |
| Other | 147,062 | 283,409 |
| Purchase of capital assets (Schedule 8) | (2,861) | (1,200) |
| Transfer of capital assets from another department | (35) | - |
| Other, net | (19,046) | 837 |
| Cash provided by (used for) investing transactions | 13,716 | (227,877) |
| **Financing transactions** | | |
| Debt issues | 23,970,385 | 13,726,938 |
| Debt retirement | (24,620,411) | (15,997,533) |
| Net transfer to general revenues | (6,350,428) | (4,042,538) |
| Cash used for financing transactions | (7,000,454) | (6,313,133) |
| **Net cash provided (used)** | 10,269 | (320,336) |
| **Cash (bank overdraft) at beginning of year** | (254,306) | 66,030 |
| **Bank overdraft at end of year** | $ (244,037) | $ (254,306) |

The accompanying notes and schedules are part of these financial statements.

DEPARTMENT OF TREASURY
STATEMENT OF FINANCIAL POSITION
MARCH 31, 1999

| | In thousands 1999 | 1998 |
|---|---|---|
| **Assets** | | |
| Accounts and accrued interest receivable (Schedule 9) | $ 902,891 | $ 928,465 |
| Loans and advances to government entities (Schedule 10) | 804,374 | 713,414 |
| Other loans, advances and investments (Schedule 11) | 307,408 | 448,169 |
| Capital assets (Schedule 12) | 4,902 | 2,846 |
| | $ 2,019,575 | $ 2,092,894 |
| **Liabilities** | | |
| Bank overdraft | $ 244,037 | $ 254,306 |
| Accounts and accrued interest payable (Schedule 13) | 447,137 | 464,288 |
| Unmatured debt (Schedule 14) | 13,064,118 | 13,352,520 |
| Pension obligations (Schedule 15) | 1,026,851 | 1,082,103 |
| Other accrued liabilities (Schedule 16) | 117,470 | 149,246 |
| | 14,899,613 | 15,302,463 |
| **Net Liabilities** | | |
| Net liabilities at beginning of year | (13,209,569) | (15,677,854) |
| Net operating results | 6,679,959 | 6,510,823 |
| Net transfer to general revenues | (6,350,428) | (4,042,538) |
| Net liabilities at end of year | (12,880,038) | (13,209,569) |
| | $ 2,019,575 | $ 2,092,894 |

The accompanying notes and schedules are part of these financial statements.

## DEPARTMENT OF TREASURY
## NOTES TO THE FINANCIAL STATEMENTS
## FOR THE YEAR ENDED MARCH 31, 1999

Note 1 Authority

The Department of Treasury (the Department) operates under the authority of the Government Organization Act, Statutes of Alberta 1994, as amended.

Note 2 Purpose

The Department's core functions are to provide analysis and recommendations to the Provincial Treasurer and Treasury Board, maintain a framework that fosters government accountability, administer and collect tax revenue, manage the province's financial assets and liabilities, and foster a fair and efficient financial marketplace.

Note 3 Summary of Significant Accounting Policies and Reporting Practices

These financial statements are prepared in accordance with the following accounting policies that have been established by government for all departments. The recommendations of the Public Sector Accounting Board of the Canadian Institute of Chartered Accountants are the primary source for the disclosed basis of accounting. Recommendations of the Accounting Standards Board of the Canadian Institute of Chartered Accountants, other authoritative pronouncements, accounting literature, and published financial statements relating to either the public sector or analogous situations in the private sector are used to supplement the recommendations of the Public Sector Accounting Board where it is considered appropriate.

**(a) Reporting Entity**

The reporting entity is the Department, which is part of the Ministry of Treasury and for which the Provincial Treasurer is accountable. Other entities reporting to the Provincial Treasurer include the Alberta Heritage Foundation for Medical Research Endowment Fund, the Alberta Heritage Savings Trust Fund, the Alberta Heritage Scholarship Fund, the Alberta Risk Management Fund, the Utility Companies Income Tax Rebates Fund, Alberta Insurance Council, Alberta Municipal Financing Corporation, Alberta Pensions Administration Corporation, Alberta Securities Commission, Alberta Government Telephones Commission and its subsidiaries, Alberta Treasury Branches and its subsidiary, Credit Union Deposit Guarantee Corporation and its subsidiary, N.A. Properties (1994) Ltd., Chembiomed Ltd., and Gainers Inc. The activities of these organizations are not included in these financial statements.

Since significant financial transactions of the Ministry are reported outside the departmental financial statements, the Ministry financial statements provide a more comprehensive accounting of the financial position and results of the Ministry's operations. The Ministry Annual Report provides a more complete picture of the responsibilities for which the Provincial Treasurer is accountable.

All departments of the Government of Alberta operate within the General Revenue Fund (the Fund). The Fund is administered by the Provincial Treasurer. All cash receipts of departments are deposited into the Fund and all cash disbursements made by departments are paid from the Fund. Net transfer to general revenues is the difference between all cash deposits by other departments and all cash disbursements made on their behalf by the Department of Treasury.

**(b) Basis of Financial Reporting**

**Revenues**

All revenues are reported on the accrual method of accounting. Corporate income tax receipts in abeyance are recorded as accounts payable.

**Internal Government Transfers**

Internal government transfers are transfers between entities within the government reporting entity where the entity making the transfer does not receive any goods or services directly in return.

**Dedicated Revenue**

Dedicated revenue initiatives provide a basis for authorizing spending. Dedicated revenues must be shown as credits or recoveries in the details of the Government Estimates for a supply vote. If actual dedicated revenues are less than budget and total voted expenses are not reduced by an amount sufficient to cover the deficiency in dedicated revenues, the following year's expense budget is reduced. If actual dedicated revenues exceed budget, the Department may, with the approval of the Treasury Board, use the excess revenue to fund additional expenses on the program. Schedule 2 discloses information on the Department's dedicated revenue initiatives.

**Expenses**

Expenses represent the costs of resources consumed during the year on the Department's operations. Expenses include amortization of capital assets.

Pension costs included in these statements comprise the cost of employer contributions for current service of employees during the year and additional government and employer contributions for employees' service relating to prior years.

Certain expenses, primarily for office space and legal advice, incurred on behalf of the Department by other Ministries are not reflected in the statement of operations.

**Valuation Adjustments**

Valuation adjustments include changes in the valuation allowances used to reflect financial assets at their net recoverable or other appropriate value. Valuation adjustments also represent the change in management's estimate of future payments arising from obligations relating to guarantees, indemnities, pension obligations, and accrued employee vacation entitlements.

Valuation adjustments for pension obligations include interest on the Department's share of the unfunded liability, the amortization of deferred adjustments over the expected average remaining service life of employees, and the effect of the change in the ratio used to allocate a plan's total unfunded liability to participating entities.

**Assets**

Financial assets of the Department are limited to financial claims, such as advances to and receivables from other organizations, employees and other individuals.

Loans are reported at their face value except for loans made on significantly concessionary terms which are discounted by the amount of concessions. The amount of the discount is amortized to revenue over the term of the loan, except when the collectibility of either the principal or interest related to the loan transaction is not reasonably assured. The stated value of loans is estimated to approximate fair value.

Investments are recorded at cost, except for investments in wholly owned provincial corporations operating as commercial enterprises which are valued on the equity basis. Where there has been a loss in value of an investment that is other than a temporary decline, the investment is written down to recognize the loss. The written down value is deemed to be the new cost.

Capital assets of the Department are recorded at historical cost and amortized on a straight line basis over the estimated useful lives of the assets. The threshold for capitalizing new systems development is $100,000 and the threshold for all other capital assets is $15,000. Assets acquired by right are not included. In addition, donated capital assets are recorded at nil cost.

**Liabilities**

Liabilities include all financial claims payable by the Department at fiscal year end. Certain liabilities, such as pension obligations, are reflected in these financial statements on behalf of all departments.

**Net Liabilities**

Net liabilities represents the difference between the value of assets held by the Department and its liabilities.

**Measurement Uncertainty**

Estimates are used in accruing revenues and expenses in circumstances where the actual accrued revenues and expenses are unknown at the time the financial statements are prepared. Uncertainty in the determination of the amount at which an item is recognized in financial statements is known as measurement uncertainty. Such uncertainty exists when there is a variance between the recognized amount and another reasonably possible amount, as there is whenever estimates are used.

Measurement uncertainty that is material to these financial statements exists in the accrual of personal and corporate income taxes, provisions for pensions and loans and advances. The nature of the uncertainty in these items arises from several factors such as the effect on accrued taxes of the verification of taxable income; the effect on accrued pension obligations of actual experience compared to assumptions; and the effect on loans and advances of actual collectibility and changes in economic conditions. While best estimates have been used for reporting items subject to measurement uncertainty, management considers that it is possible, based on existing knowledge, that changes in future conditions in the near term could require a material change in the recognized amounts. Near term is defined as a period of time not to exceed one year from the date of the financial statements.

### (c) Change in Accounting Policy

Pension expense associated with the Teachers' Pension Plan that was previously reported in the financial statements of the Department of Treasury on behalf of the Department of Education is now reported by the Department of Education. Net operating results increased by $42,509,000 (1998 $199,107,000) as a result of this change.

The Department no longer reports liabilities associated with Teachers' Pension Plan entitlements. These liabilities are now reported in the financial statements of the Department of Education. Pension obligations and net liabilities have decreased by $3,783,184,000 (1998 $3,804,500,000) as a result of this change.

This change has been applied retroactively and prior periods have been restated to reflect the change.

Note 4 Liability Risk Management

The objective of the Department's liability management program is to achieve the lowest cost on debt within an acceptable degree of variability of debt servicing costs. In order to achieve this objective, the Department manages four risks - interest rate risk, currency exchange risk, credit risk, and refunding risk. The Department manages these four risks within approved policy guidelines. The management of these risks and the policy guidelines apply to the Department's unmatured debt, excluding debt raised to fund requirements of provincial corporations and regulated funds. Debt of provincial corporations and regulated funds is managed separately in relation to their assets.

The policy guideline for interest rate risk is that Canadian dollar floating rate debt should be between 38 per cent and 50 per cent of total Canadian dollar debt. The policy guideline for currency exchange risk is that there be no exposure to currencies other than United States dollars. Further, the unhedged U.S. dollar debt should not exceed US$3,000,000,000.

Credit risk relating to swaps is minimal as management deals only with the most credit worthy counterparties. The policy guideline for refunding risk is that term debt maturities should not exceed $3,500,000,000 in any fiscal year, excluding early redemption of Alberta Capital Bonds and Alberta Savings Certificates.

These policies were complied with during the year.

Note 5 Commitments and Contingencies

Set out below are details of commitments to organizations outside the Department and contingencies resulting from guarantees, indemnities and litigation, other than those reported as liabilities and shown in Schedule 16.

Management considers that the contingencies will not result in any material adverse effect on the Department. Any losses arising from the settlement of contingencies are treated as current year expenses.

### (a) Credit Union Act

The Credit Union Deposit Guarantee Corporation, operating under the authority of the Credit Union Act, guarantees the repayment of all deposits with Alberta credit unions, including accrued interest. The Credit Union Act provides that the Province, through the Department, will ensure that this obligation of the Corporation is carried out. As at December 31, 1998, credit unions in Alberta held deposits totalling $4,771,124,000 (1997 $4,424,265,000). Substantial assets are available to safeguard the Department from risk of loss arising from its potential obligation under the Act.

### (b) Other Commitments

Commitments to outside organizations in respect of contracts entered into before March 31, 1999 amounted to $6,456,000 (1998 $612,000). These commitments will become expenses of the Department when terms of the contracts are met. Payments in respect of these contracts and agreements are subject to the voting of supply by the Legislature.

### (c) Debenture, Deposit and Loan Guarantees

Guaranteed liabilities at March 31, 1999 of government entities amounting to $14,087,799,000 (1998 $14,493,627,000), and other guarantees amounting to $301,880,000 (1998 $468,646,000) are analyzed in Schedules 17 and 18 respectively. These schedules are included with the financial statements because payments under debenture and loan guarantees are a statutory charge on the Department. Payments under the guarantee of Alberta Treasury Branches deposits would also be made by the Department, under authority of a supply vote.

### (d) Legal Actions

At March 31, 1999, the Department was named as defendant in various legal actions. The total claimed in specific legal actions amounts to approximately $146,201,000 (1998 $161,237,000).

The resulting loss, if any, from these claims cannot be determined.

Note 6 Valuation of Financial Assets and Liabilities

Fair value is the amount of consideration agreed upon in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act.

The fair values of cash, accrued interest, receivables and payables, are estimated to approximate their book values.

Fair values of loans and advances are not reported due to there being no organized financial market for the instruments and it is not practicable within constraints of timeliness or cost to estimate the fair values with sufficient reliability.

The fair value of unmatured debt is an approximation of its fair value to the holder.

At the year end, the fair values of assets and liabilities denominated in a foreign currency are translated at the year end exchange rate.

Note 7 Related Party Transactions

As explained in Notes 2 and 3(a), the Department is responsible for handling all departments' cash transactions. As a result, the Department engages in transactions with its own funds and agencies and with all other departments and their funds and agencies in the normal course of operations.

The Deputy Provincial Treasurer is a director of Alberta Pensions Administration Corporation and Alberta Municipal Financing Corporation. During the year, the Controller was a director of PSC Payment Systems Corporation. Alberta Pensions Administration Corporation is wholly owned, Alberta Municipal Financing Corporation is 70 per cent owned and, until March 31, 1999, PSC Payment Systems Corporation was 40 per cent owned by the Government of Alberta, through the Department. The government's ownership interest in PSC Payment Systems Corporation was sold on March 31, 1999 for $2,550,000, which is included in miscellaneous other revenue. Neither of the officials referred to above received any benefit during the year, in cash or in kind, as a result of these directorships.

The investment in Alberta Municipal Financing Corporation is recorded at cost (see Schedule 11) because the Corporation has the power to pay its retained earnings, which amounted to $318,602,000 at December 31, 1998 (1997 $333,505,000), to municipal and other shareholders which have borrowed money from the Corporation. During the 1998-99 fiscal year, the Department, on behalf of the Department of Education, paid $215,844,000 (1998 $325,416,000) to the Corporation to satisfy interest and principal repayment requirements of school board debentures. The investments in and transactions with Alberta Pensions Administration Corporation and PSC Payment Systems Corporation are not significant, on both a cost and equity basis.

Accommodations, legal, telecommunications and personnel services were provided to the Department during the year by other government organizations at no cost.

The Department and its employees paid certain taxes and fees set by regulation for permits, licences, and other rights. These amounts were incurred in the normal course of business and reflect charges applicable to all users.

Note 8 Trust Funds Under Administration

The Department administers trust funds that are regulated funds consisting of public money over which the Legislature has no power of appropriation. Because the Province has no equity in the funds and administers them for the purpose of various trusts, they are not included in the Department's financial statements.

As at March 31, 1999, trust funds under administration were as follows:

| | In thousands | |
|---|---|---|
| | 1999 | 1998 |
| Local Authorities Pension Plan Fund | $ 7,771,333 | $ 7,571,914 |
| Public Service Pension Plan Fund | 3,674,083 | 3,579,475 |
| The Workers' Compensation Board Accident Fund | 2,703,227 | 2,909,897 |
| Universities Academic Pension Plan Fund | 1,566,196 | 1,562,932 |
| Management Employees Pension Plan Fund | 1,334,290 | 1,279,737 |
| Special Forces Pension Plan Fund | 856,245 | 841,281 |
| Regional Health Authorities and various health institutions construction accounts | 164,866 | 103,297 |
| Other | 76,048 | 275,148 |
| | $ 18,146,288 | $ 18,123,681 |

Note 9 Payments Based on Agreement

During the year, the Department was a party to two agreements for which expenses were incurred by the Department under authority of the Financial Administration Act, Section 29.1. One agreement is to pay the salaries of Treasury employees seconded to Alberta Pensions Administration Corporation. The salaries paid are recovered in full from the Corporation. The other agreement is to make an annual contribution of $245,000 for the Canadian Fuel Tax Uniformity Project, to be recovered in full from fuel tax revenue.

Only the amounts receivable or payable at the year end under these agreements are reflected in these financial statements. Revenues and expenses are not included. Accounts receivable of $33,000 (1998 $276,000) from Alberta Pensions Administration Corporation and accounts payable of $94,000 (1998 $nil) for the Canadian Fuel Tax Uniformity Project are reflected in the statement of financial position.

Amounts paid and payable under agreements with the Department of Treasury for the year ended March 31, 1999 were as follows:

| | In thousands | |
|---|---|---|
| | 1999 | 1998 |
| Alberta Pensions Administration Corporation Payroll | $ 3,055 | $ 4,331 |
| Canadian Fuel Tax Uniformity Project | 131 | - |
| International Fuel Tax Agreement | - | 1,470 |
| | $ 3,186 | $ 5,801 |

Note 10 Uncertainty Due to the Year 2000

The year 2000 issue is the result of some computer systems using two digits rather than four to define the applicable year. Government computer systems that have date sensitive software may recognize a date using "00" as the year 1900 rather than the year 2000, which could result in miscalculations or system failures. In addition, similar problems may arise in some systems if certain dates in 1999 are not recognized as a valid date or are recognized to represent something other than a date. The effects of the year 2000 issue may be experienced before, on, or after January 1, 2000. If not addressed, the effect on operations and financial reporting may range from minor errors to significant systems failure that could affect the ability to conduct some government operations. Despite the government's efforts to address this issue, it is not possible to be certain that all aspects of the year 2000 issue affecting the government, including those related to the efforts of customers, suppliers and other third parties, will be fully resolved.

Note 11 Comparative Figures

Certain 1998 figures have been reclassified to conform to the 1999 presentation.

Due from general revenues reported in 1998 has been reclassified to net liabilities in 1999. The change in net liabilities reported on the statement of financial position includes net transfer to general revenues. As a result, the net contribution to general revenues as previously reported is no longer required.

Note 12 Approval of Financial Statements

These financial statements were approved by the Acting Corporate Secretary and the Deputy Provincial Treasurer.

DEPARTMENT OF TREASURY
SCHEDULES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED MARCH 31, 1999

Schedule 1

REVENUES

| | In thousands | | |
|---|---|---|---|
| | 1999 | | 1998 |
| | Budget | Actual | Actual |
| Internal government transfers: | | | |
| Transfer from the Alberta Heritage Savings Trust Fund | $ 716,200 | $ 932,013 | $ 922,346 |
| Income taxes: | | | |
| Personal income tax | 3,835,048 | 4,600,762 | 3,876,571 |
| Corporate income tax | 1,642,287 | 1,658,917 | 1,848,528 |
| Corporate income tax cushion | (164,229) | - | - |
| | 5,313,106 | 6,259,679 | 5,725,099 |
| Other taxes: | | | |
| Fuel tax | 570,000 | 546,918 | 557,980 |
| Tobacco tax | 345,000 | 341,333 | 329,920 |
| Insurance corporations tax | 112,047 | 101,555 | 121,532 |
| Hotel room tax | 41,000 | 44,614 | 42,370 |
| Financial institutions capital tax | 39,315 | 31,438 | 36,467 |
| | 1,107,362 | 1,065,858 | 1,088,269 |
| Non-renewable resource revenue: | | | |
| Royalty tax credit | (233,000) | (249,486) | (225,406) |
| Transfers from Government of Canada: | | | |
| Unconditional subsidy | 3,931 | 3,692 | 3,931 |
| Investment income: | | | |
| Farm credit stability program | 39,700 | 37,680 | 58,804 |
| Other | 52,458 | 27,545 | 26,302 |
| | 92,158 | 65,225 | 85,106 |
| Fees, permits and licences: | | | |
| Insurance companies, agents and brokers | 800 | 249 | 537 |
| Other | 1,204 | 589 | 1,399 |
| | 2,004 | 838 | 1,936 |
| Transfers from government enterprises: | | | |
| Alberta Government Telephones Commission | 900 | 10,137 | 8,390 |
| Revolving funds | - | - | 958 |
| | 900 | 10,137 | 9,348 |
| Other: | | | |
| Sale of assets | 2,000 | - | |
| Refunds of expenditure | 588 | 3,778 | 1,109 |
| Miscellaneous | 6,574 | 12,836 | 7,762 |
| | 9,162 | 16,614 | 8,871 |
| | $ 7,011,823 | $ 8,104,570 | $ 7,619,500 |

Schedule 2

## DEDICATED REVENUE INITIATIVES

| | In thousands | | |
|---|---|---|---|
| | 1999 | | 1998 |
| | Authorized Budget | Actual | Actual |
| **Tax and revenue administration:** | | | |
| Dedicated revenue | $ 631 | $ 943 | $ - |
| Expense | 13,502 | 13,055 | 12,246 |
| Net expense | $ 12,871 | $ 12,112 | $ 12,246 |
| **Finance:** | | | |
| Dedicated revenue | $ 1,948 | $ 2,137 | $ - |
| Expense | 7,814 | 7,327 | 19,760 |
| Net expense | $ 5,866 | $ 5,190 | $ 19,760 |
| **Investment management:** | | | |
| Dedicated revenue | $ 3,999 | $ 4,169 | $ - |
| Expense | 4,099 | 4,483 | - |
| Net expense | $ 100 | $ 314 | $ - |
| **Totals:** | | | |
| Dedicated revenue | $ 6,578 | $ 7,249 | $ - |
| Expense | 25,415 | 24,865 | 32,006 |
| Net expense | $ 18,837 | $ 17,616 | $ 32,006 |

Dedicated revenue initiatives provide a basis for authorizing spending. Dedicated revenues must be shown as credits or recoveries in the details of the Government Estimates for a supply vote. If actual dedicated revenues are less than budget and total voted expenses are not reduced by an amount sufficient to cover the deficiency in dedicated revenues, the following year's expense budget is reduced. If actual dedicated revenues exceed budget, the Department may, with the approval of the Treasury Board, use the excess revenue to fund additional expenses on the program.

Following is a brief description of each dedicated revenue initiative:

Tax and revenue administration: Collects debts owing to the Crown on behalf of government departments having no collection infrastructure or having accounts that are difficult to collect.

Finance: Provides banking, securities administration and systems support services to various public sector investment funds. Fees are based on cost recovery.

Investment management: Manages the investments of various public sector investment funds. Fees are based on cost recovery.

The revenue and expense of each initiative's dedicated revenue and expense are reported in the statement of operations.

Schedule 3

BUDGET

In thousands
For the year ended March 31, 1999

| | 1998-99 Estimates (a) | Adjustments and Reallocations (b) | 1998-99 Budget | Voted Supplementary (a) | 1998-99 Authorized Budget |
|---|---|---|---|---|---|
| Revenues | | | | | |
| Internal government transfers | $ 716,200 | $ - | $ 716,200 | $ - | $ 716,200 |
| Income taxes | 5,313,106 | - | 5,313,106 | - | 5,313,106 |
| Other taxes | 1,107,362 | - | 1,107,362 | - | 1,107,362 |
| Non-renewable resource revenue | | | | | |
| Royalty tax credit | (233,000) | - | (233,000) | - | (233,000) |
| Transfers from Government of Canada | 3,931 | - | 3,931 | - | 3,931 |
| Investment income | 92,158 | - | 92,158 | | 92,158 |
| Fees, permits and licences | 2,004 | - | 2,004 | - | 2,004 |
| Transfers from government enterprises | 900 | - | 900 | - | 900 |
| Other | 9,162 | - | 9,162 | 1,182 | 10,344 |
| | 7,011,823 | - | 7,011,823 | 1,182 | 7,013,005 |
| Expenses | | | | | |
| Voted: | | | | | |
| Ministry support services | 4,970 | - | 4,970 | 775 | 5,745 |
| Revenue collection and rebates | 13,502 | - | 13,502 | - | 13,502 |
| Financial management and planning | 17,685 | - | 17,685 | 1,182 | 18,867 |
| | 36,157 | - | 36,157 | 1,957 | 38,114 |
| Statutory: | | | | | |
| Corporate tax interest refunds | 13,000 | - | 13,000 | - | 13,000 |
| Farm credit stability program | 6,500 | - | 6,500 | - | 6,500 |
| Pension liability funding | 155,500 | (63,500) | 92,000 | - | 92,000 |
| Debt servicing costs | 1,094,000 | - | 1,094,000 | - | 1,094,000 |
| | 1,269,000 | (63,500) | 1,205,500 | - | 1,205,500 |
| Valuation adjustments | 30,000 | (97,000) | (67,000) | - | (67,000) |
| | 1,335,157 | (160,500) | 1,174,657 | 1,957 | 1,176,614 |
| Net operating results | $ 5,676,666 | $ 160,500 | $ 5,837,166 | $ (775) | $ 5,836,391 |

(a) Government Estimates were approved on March 26, 1998 and Supplementary Estimates were approved on March 8, 1999. Treasury Board approval is pursuant to section 29(1.1) of the Financial Administration Act.

(b) Adjustments and reallocations consist of: $(63,500,000) of pension liability funding for the Teachers' Pension Plan transferred to the Department of Education as a result of the change in accounting policy referred to in Note 3(c); $76,000,000 for pension provisions referred to in Budget '98 but not included in the Estimates; and $(173,000,000) for pension provisions relating to the Teachers' Pension Plan transferred to the Department of Education as a result of the change in accounting policy referred to in Note 3(c).

Schedule 4

## COMPARISON OF EXPENSES AND DISBURSEMENTS BY ELEMENT TO AUTHORIZED BUDGET

In thousands

| | 1998-99 Budget | Voted Supplementary | 1998-99 Authorized Budget | 1998-99 Actual Expense | Unexpended (Over Expended) |
|---|---|---|---|---|---|
| Expenses: | | | | | |
| Voted Expenses | | | | | |
| Program 1 - Ministry Support Services | | | | | |
| 1.0.1 Provincial Treasurer's Office | $ 312 | $ - | $ 312 | $ 298 | $ 14 |
| 1.0.2 Deputy Provincial Treasurer's Office | 249 | - | 249 | 289 | (40) |
| 1.0.3 Financial and Support Services | 1,656 | - | 1,656 | 1,833 | (177) |
| 1.0.4 Human Resource Services | 264 | - | 264 | 300 | (36) |
| 1.0.5 Corporate Information Management Services | 1,472 | - | 1,472 | 1,497 | (25) |
| 1.0.6 Records Management | 338 | - | 338 | 364 | (26) |
| 1.0.7 Communications | 422 | - | 422 | 317 | 105 |
| 1.0.8 Standing Policy Committee on Financial Planning and Human Resources | 95 | - | 95 | 88 | 7 |
| 1.0.9 Regulatory Reform | 162 | - | 162 | 131 | 31 |
| 1.0.10 Achievement Awards | - | 775 | 775 | 664 | 111 |
| | 4,970 | 775 | 5,745 | 5,781 | (36) |
| Program 2 - Revenue Collection and Rebates | | | | | |
| 2.0.1 Tax and Revenue Administration | 13,502 | - | 13,502 | 13,055 | 447 |
| Program 3 - Financial Management and Planning | | | | | |
| 3.0.1 Office of Budget and Management | 6,954 | | 6,954 | 7,467 | (513) |
| 3.0.2 Finance | 7,465 | 349 | 7,814 | 7,327 | 487 |
| 3.0.4 Investment Management | 3,266 | 833 | 4,099 | 4,483 | (384) |
| | 17,685 | 1,182 | 18,867 | 19,277 | (410) |
| Total Voted Expenses | $ 36,157 | $ 1,957 | $ 38,114 | $ 38,113 | $ 1 |
| Statutory Expenses | | | | | |
| Corporate tax interest refunds | $ 13,000 | $ - | $ 13,000 | $ 98,253 | $ (85,253) |
| Farm credit stability program | 6,500 | | 6,500 | 6,904 | (404) |
| Small business term assistance program | - | - | - | 9 | (9) |
| Pension liability funding | 92,000 | - | 92,000 | 70,741 | 21,259 |
| Debt servicing costs | 1,094,000 | | 1,094,000 | 1,264,427 | (170,427) |
| Total Statutory Expenses | $ 1,205,500 | $ - | $ 1,205,500 | $ 1,440,334 | $ (234,834) |

| | 1998-99 Budget | Voted Supplementary | 1998-99 Authorized Budget | 1998-99 Actual Disbursements | Unexpended (Over Expended) |
|---|---|---|---|---|---|
| Disbursements: | | | | | |
| Voted Non-Budgetary Disbursements | | | | | |
| Program 3 - Financial Management and Planning | | | | | |
| 3.0.3 Pre-1995 Insurance Liability | $ 6,107 | $ - | $ 6,107 | $ 6,107 | $ - |

## EXPENSES DETAILED BY OBJECT

Schedule 5

In thousands

| | 1999 Budget | 1999 Actual | 1998 Actual |
|---|---|---|---|
| Voted: | | | |
| Salaries, wages and employee benefits | $ 23,776 | $ 24,223 | $ 17,156 |
| Supplies and services | 9,901 | 11,232 | 27,078 |
| Grants | - | 7 | - |
| Financial transactions and other | 1,587 | 1,811 | 119 |
| Amortization of capital assets | 893 | 840 | 470 |
| Total Voted Expenses | $ 36,157 | $ 38,113 | $ 44,823 |
| Statutory: | | | |
| Corporate tax interest refunds | $ 13,000 | $ 98,253 | $ 18,206 |
| Pension liability funding | 92,000 | 70,741 | 90,218 |
| Debt servicing costs | 1,094,000 | 1,264,427 | 1,186,183 |
| Other financial transactions | 6,500 | 6,913 | 10,145 |
| Total Statutory Expenses | $ 1,205,500 | $ 1,440,334 | $ 1,304,752 |

## VALUATION ADJUSTMENTS

Schedule 6

In thousands

| | 1999 Budget | 1999 Actual | 1998 Actual |
|---|---|---|---|
| Provision for doubtful accounts and loans | $ 15,000 | $ 10,261 | $ 2,817 |
| Provision for employee benefits other than pensions | - | 542 | 9,318 |
| Provision for settlement with Principal Group noteholders | - | - | (15,000) |
| Provision for guarantees and indemnities | 15,000 | (9,387) | (16,329) |
| Pension provisions | (97,000) | (55,252) | (221,704) |
| | $ (67,000) | $ (53,836) | $ (240,898) |

## SALARY AND BENEFITS DISCLOSURE

Schedule 7

| | 1999 Salary [1] | 1999 Benefits and Allowances | 1999 Total | 1998 Total |
|---|---|---|---|---|
| Senior Officials | | | | |
| Deputy Provincial Treasurer | $ 157,275 | $ 12,506 | $ 169,781 | $ 132,738 |
| Associate Deputy Provincial Treasurer | 40,685 | 3,230 | 43,915 | - |
| Controller | 117,205 | 13,220 | 130,425 | 114,500 |
| Executives | | | | |
| Assistant Deputy Provincial Treasurer - Revenue [6] | 106,676 | 14,260 | 120,936 | 110,543 |
| Assistant Deputy Provincial Treasurer - Treasury Operations | 108,663 | 14,011 | 122,674 | 112,834 |
| Chief Investment Officer | 161,158 | 15,060 | 176,218 | 118,920 |
| Corporate Secretary | 94,784 | 28,842 | 123,626 | 105,892 |

Schedule 7 (continued)

## SALARY AND BENEFITS DISCLOSURE (continued)

(1) Salary includes regular base pay, bonuses, overtime and lump sum payments.

(2) Benefits and allowances include the employer's share of benefits provided, including pensions, health care, dental, group life insurance, long-term disability plans, workers' compensation, payments in lieu of vacation earned but not taken, professional memberships, tuition and the learning account.

(3) Automobile provided, no amount is included in the benefits and allowances figure.

(4) Associate Deputy Provincial Treasurer appointed effective February 1, 1999 by Order in Council.

(5) Benefits and allowances include vacation payouts as follows: Assistant Deputy Provincial Treasurer - Treasury Operations 1999 - $nil (1998 - $3,365) and Chief Investment Officer 1999 - $nil (1998 - $1,732). In 1999 the vacation payout to the Corporate Secretary on termination was $14,694.

(6) The 1998 salaries and benefits have been adjusted to reflect additional bonus amounts undecided at March 31, 1998, which were included in the management category total.

Schedule 8

## PURCHASE OF CAPITAL ASSETS

| | In thousands | | |
|---|---|---|---|
| | 1999 | | 1998 |
| | Budget | Actual | Actual |
| Program 1 - Ministry Support Services | | | |
| 1.0.5 Corporate Information Management Services | $ 475 | $ 167 | $ 36 |
| Program 2 - Revenue Collection and Rebates | | | |
| 2.0.1 Tax and Revenue Administration | 2,596 | 2,495 | 1,089 |
| Program 3 - Financial Management and Planning | | | |
| 3.0.1 Office of Budget and Management | - | - | 75 |
| 3.0.2 Finance | 325 | 199 | - |
| | 325 | 199 | 75 |
| | $ 3,396 | $ 2,861 | $ 1,200 |

Schedule 9

## ACCOUNTS AND ACCRUED INTEREST RECEIVABLE

| | In thousands | |
|---|---|---|
| | 1999 | 1998 |
| Personal income tax | $ 462,467 | $ 330,748 |
| Corporate income tax | 206,633 | 209,713 |
| Alberta Heritage Savings Trust Fund | 68,013 | 198,346 |
| Alberta Government Telephones Commission | 66,079 | 58,942 |
| Fuel tax | 45,242 | 48,813 |
| Insurance corporations tax | 24,669 | 36,618 |
| Accrued interest receivable | 15,739 | 14,856 |
| Financial institutions capital tax | 7,998 | 13,144 |
| Tobacco tax | 3,540 | 3,584 |
| Forward contracts | | 3,468 |
| Other | 6,589 | 14,336 |
| | 906,969 | 932,568 |
| Less: Allowance for doubtful accounts | 4,078 | 4,103 |
| | $ 902,891 | $ 928,465 |

## LOANS AND ADVANCES TO GOVERNMENT ENTITIES

Schedule 10

| | In thousands | |
|---|---|---|
| | 1999 | 1998 |
| Alberta Social Housing Corporation | $ 432,224 | $ 456,380 |
| Agriculture Financial Services Corporation | 246,179 | 58,117 |
| Alberta Opportunity Company | 85,747 | 71,123 |
| Environmental Protection and Enhancement Fund | 40,000 | - |
| Public Trustee | 224 | 224 |
| Alberta School Foundation Fund | - | 73,000 |
| Advances to revolving funds | - | 54,570 |
| | $ 804,374 | $ 713,414 |

## OTHER LOANS, ADVANCES AND INVESTMENTS

Schedule 11

| | In thousands | |
|---|---|---|
| | 1999 | 1998 |
| Loans and advances: | | |
| Farm Credit Stability Act | $ 290,269 | $ 425,230 |
| Centennial Food Corporation | 13,850 | 14,250 |
| Pratt & Whitney Canada Ltd. | 4,187 | 4,465 |
| Board of Governors of the University of Alberta | 3,218 | 3,474 |
| Accountable advances | 1,392 | 1,357 |
| University of Lethbridge Students' Union | 1,362 | 1,480 |
| University of Calgary Students' Union | 1,249 | 1,506 |
| Advances under the Municipal Land Loans Act | 1,070 | 2,025 |
| Implemented guarantees and indemnities | 438 | 488 |
| Judgement debts | 286 | 419 |
| University of Alberta Students' Union | 233 | 455 |
| Loans to municipalities | 155 | 299 |
| Small Business Term Assistance Act | 4 | 486 |
| Canadian Western Bank | - | 4 |
| | 317,713 | 455,938 |
| Less: Allowance for doubtful loans and advances | 10,650 | 8,000 |
| | 307,063 | 447,938 |
| Investments: | | |
| New Noble Services Ltd. | 186 | 186 |
| N.A. Properties (1994) Ltd. | 114 | - |
| Alberta Municipal Financing Corporation | 45 | 45 |
| | 345 | 231 |
| | $ 307,408 | $ 448,169 |

## CAPITAL ASSETS

Schedule 12

| | | In thousands | | | |
|---|---|---|---|---|---|
| | | 1999 | | | 1998 |
| | Estimated Useful Life | Cost | Accumulated Amortization | Net Book Value | Net Book Value |
| Equipment | 10 years | $ 616 | $ 474 | $ 142 | $ 138 |
| Computer hardware and software | 5 years | 22,407 | 17,647 | 4,760 | 2,708 |
| | | $ 23,023 | $ 18,121 | $ 4,902 | $ 2,846 |

## ACCOUNTS AND ACCRUED INTEREST PAYABLE

Schedule 13

| | In thousands | |
|---|---|---|
| | 1999 | 1998 |
| Accrued interest on unmatured debt | $ 323,297 | $ 331,924 |
| Corporate income tax receipts in abeyance | 103,105 | 86,026 |
| Alberta Social Housing Corporation | 2,338 | 2,572 |
| Other | 18,397 | 43,766 |
| | $ 447,137 | $ 464,288 |

## UNMATURED DEBT

Schedule 14

| | In thousands | | | | | |
|---|---|---|---|---|---|---|
| | 1999 | | | | 1998 | |
| | Effective Rate (a)(b)(c) | Modified Duration (d) | Book Value (a) | Fair Value (a) | Book Value (a) | Fair Value (a) |
| | % | years | | | | |
| Canadian dollar debt and fully hedged foreign currency debt: | | | | | | |
| Floating rate and short-term fixed rate debt (e) | 6.11 | 0.29 | $ 3,344,403 | $ 3,360,000 | $ 3,017,534 | $ 3,069,000 |
| Fixed rate long-term debt (f) | 7.51 | 4.39 | 4,690,998 | 5,446,000 | 5,272,810 | 6,026,000 |
| | 6.93 | 2.81 | 8,035,401 | 8,806,000 | 8,290,344 | 9,095,000 |
| Unhedged U.S. dollar debt (g): | | | | | | |
| Floating rate and short-term fixed rate debt (e) | 4.90 | 0.16 | 2,363,715 | 2,469,000 | 3,046,178 | 3,224,000 |
| Fixed rate long-term debt | 7.37 | 1.99 | 1,913,953 | 2,105,000 | 1,487,174 | 1,682,000 |
| | 6.02 | 1.00 | 4,277,668 | 4,574,000 | 4,533,352 | 4,906,000 |
| | 6.61 | 2.20 | 12,313,069 | 13,380,000 | 12,823,696 | 14,001,000 |
| Provincial corporation and regulated fund Canadian dollar debt (h) | 5.67 | 7.07 | 751,049 | 778,000 | 528,824 | 619,000 |
| | 6.56 | 2.46 | $ 13,064,118 | $ 14,158,000 | $ 13,352,520 | $ 14,620,000 |

UNMATURED DEBT (continued)

(a) Book value represents the amount the Department owes. Fair value is an approximation of market value to the holder. The book value, fair value and weighted average effective rate include the effect of interest rate and currency rate swaps. For non-marketable issues, the effective rate and fair value are determined by reference to yield curves for comparable quoted issues.

(b) Weighted average effective rates on unhedged U.S. dollar debt are based upon debt stated in U.S. dollars.

(c) Weighted average effective rate on total unmatured debt is on debt inclusive of deferred exchange losses on unhedged U.S. dollar debt (see note (g)).

(d) Modified duration is the weighted average term to maturity of the security's cash flows (i.e., interest and principal) and is a measure of price volatility; the greater the modified duration of a bond, the greater its percentage price volatility.

(e) Floating rate debt includes short-term debt, term debt with less than one year remaining to maturity, and term debt with interest rate reset within a year.

(f) Canadian dollar fixed rate debt includes $678,696,000 (1998 $678,696,000) held by the Canada Pension Plan Investment Fund.

(g) Unhedged U.S. dollar debt is translated into Canadian dollars at the March 31 noon exchange rate of $1.5092 per U.S. dollar (1998 $1.4166 per U.S. dollar). Deferred exchange losses on unhedged U.S. dollar debt amounted to $149,000,000 at March 31, 1999 (1998 $168,000,000). Amortization of deferred exchange losses amounted to $302,000,000 for the year ended March 31, 1999 (1998 $154,000,000).

(h) Provincial corporation and regulated fund Canadian dollar debt is debt borrowed by the Department on behalf of Provincial corporations and the Environmental Protection and Enhancement Fund.

Debt principal repayment requirements at par in each of the next five years, including short-term debt maturing in 1999-2000, and thereafter are as follows:

| | | |
|---|---|---|
| 1999-2000 | $2,730,000,000 | (includes U.S. $403,000,000 unhedged) |
| 2000-01 | $2,226,000,000 | (includes U.S. $800,000,000 unhedged) |
| 2001-02 | $1,462,000,000 | (includes U.S. $376,000,000 unhedged) |
| 2002-03 | $ 903,000,000 | (includes U.S. $500,000,000 unhedged) |
| 2003-04 | $1,810,000,000 | (includes U.S. $500,000,000 unhedged) |
| Thereafter | $4,135,000,000 | (includes U.S. $362,000,000 unhedged) |

Some of the debt has call provisions. Years to maturity reflect original maturity date and not early call date. Debt with call provisions occurring in under one year is $450,000,000, and in one to five years is $285,000,000.

**Derivative financial instruments**

The Department uses interest rate swaps and currency rate swaps and contracts to manage the interest rate risk and currency exposure associated with unmatured debt. In addition, forward interest rate agreements are used to manage interest rate exposure in the short term. Associated with these instruments are credit risks that could expose the Department to potential losses. Credit risk relates to the possibility that a loss may occur from the failure of another party to perform according to the terms of a contract. Credit exposure to counterparties is a fraction of the notional principal amount, as shown in the table below. The Department minimizes its credit risk associated with these contracts by dealing with only the most credit worthy counterparties.

Interest rate swaps involve the exchange of a series of interest payments, either at a fixed or floating rate, based upon a contractual or notional principal amount. An interest rate swap agreement based upon a notional amount involves no exchange of underlying principal. The notional amount serves as the basis for determining the exchange of interest payments. At March 31, 1999, interest rate swap agreements were being used primarily to convert fixed interest rate payments to floating rates.

Cross currency interest rate swaps involve both the swapping of interest rates and currencies.

Currency rate swaps including foreign exchange contracts involve an agreement to exchange United States dollars and other currencies into Canadian and United States dollars at an agreed upon rate and on an agreed settlement date.

The following table summarizes the Department's derivative portfolio and related credit exposure:

**Notional amount:** represents the amount to which a rate or price is applied in order to calculate the exchange of cash flows.

**Replacement cost:** represents the cost of replacing, at current market rates, all contracts which have a positive market value.

## UNMATURED DEBT (continued)

Schedule 14 (continued)

| | In thousands | | | |
|---|---|---|---|---|
| | 1999 | | 1998 | |
| | Notional Amount | Replacement Cost | Notional Amount | Replacement Cost |
| Interest rate swaps | $ 3,175,000 | $ 263,000 | $ 2,089,000 | $ 182,000 |
| Cross currency interest rate swaps | 1,037,000 | 41,000 | 1,233,000 | 31,000 |
| Currency rate swaps including foreign exchange contracts (stated in Canadian dollars) | - | - | 31,000 | 4,000 |
| | $ 4,212,000 | $ 304,000 | $ 3,353,000 | $ 217,000 |

Schedule 15

## PENSION OBLIGATIONS

Pension obligations are based upon actuarial valuations performed at least triennially using the projected benefit method pro-rated on services. The assumptions used in the valuations were adopted after consultation between the pension plan boards, the government and the actuaries, depending on the plan, and represent best estimates of future events. Each plan's future experience will inevitably vary, perhaps significantly, from the assumptions. Any differences between the actuarial assumptions and future experience will emerge as gains or losses in future valuations. Gains and losses are amortized over the expected average remaining service lives of the related employee groups.

The valuations were based upon economic assumptions, including a long-term rate of return on pension plan fund assets of 4.0 per cent over the level of price inflation for all the plans. The rate was based upon a long-term rate of return of 8 per cent and 4 per cent respectively for the Universities Academic and Special Forces plans, and 7.5 per cent and 3.5 per cent respectively for the Public Service Management (Closed Membership), Public Service, Management Employees and Local Authorities plans. Demographic assumptions used in the valuations reflect the experience of the plans.

The latest actuarial valuations were performed as at December 31, 1997 for the Public Service, Members of the Legislative Assembly, Management Employees and Local Authorities plans, as at December 31, 1996 for the Public Service Management (Closed Membership) and Universities plans, and as at December 31, 1995 for the Special Forces plan. Except for the Local Authorities plan, these actuarial valuations indicated a deficiency of net assets over actuarial present value of accrued benefits. Including deferred adjustments, unfunded liabilities were extrapolated to March 31, 1999.

A separate pension plan fund is maintained for each pension plan except for the Members of the Legislative Assembly plan Pension plan fund assets are invested in both marketable investments of organizations external to the government and in Province of Alberta bonds and promissory notes.

| | In thousands | |
|---|---|---|
| | 1999 | 1998 |
| Obligations to pension plans for current and former employees and Members of the Legislative Assembly: | | |
| Public Service Management (Closed Membership) Pension Plan (a) | $ 656,698 | $ 656,890 |
| Public Service Pension Plan (a) | 175,497 | 189,363 |
| Members of the Legislative Assembly Pension Plan (b) | 49,119 | 57,754 |
| Management Employees Pension Plan (a) | 31,107 | 48,855 |
| | 912,421 | 952,862 |
| Obligations to pension plans for employees of organizations outside the government reporting entity: | | |
| Universities Academic Pension Plan (c) | 106,041 | 101,499 |
| Special Forces Pension Plan (c) | 8,389 | 16,683 |
| Local Authorities Pension Plan (c) | - | 11,059 |
| | 114,430 | 129,241 |
| | $ 1,026,851 | $ 1,082,103 |

PENSION OBLIGATIONS (continued)

(a) The Province administers three defined benefit pension plans for substantially all of its employees. The three plans are the Public Service Management (Closed Membership), the Public Service and the Management Employees pension plans. An employee can be a member of only one plan at a time.

The Public Service Management (Closed Membership) pension plan provides benefits to former members of the Public Service Management pension plan who were retired, were entitled to receive a deferred pension or had attained 35 years of service before August 1, 1992. After all assets in the plan are exhausted, all benefits under the plan will be paid by the Department.

For Public Service, the unfunded liability for service credited prior to January 1, 1992 is being financed by additional contributions in the ratio of 62.5 per cent by the Department and 18.75 per cent each by employers and employees, over the period ending on or before December 31, 2036. Current service costs are funded by employers and employees.

For Management Employees, the unfunded liability for service credited prior to January 1, 1992 is being financed by additional contributions of 0.75 per cent for employees and such percentages by employers as will be required to eliminate the unfunded liability over the period ending on or before December 31, 2043. Current service costs are funded by employers and employees.

(b) The Department has a liability for payment of pension benefits under a defined benefit pension plan for Members of the Legislative Assembly. Active participation in this plan was terminated as of June 1993, and no benefits can be earned for service after this date. The December 31, 1997 actuarial valuation used a discount rate of 7.5 per cent and a long term inflation rate of 3.5 per cent.

(c) Under the Public Sector Pension Plans Act, the Department has or previously had obligations for payment of additional contributions under defined benefit pension plans for employees of post-secondary educational institutions and local authorities. The three plans are the Universities Academic, Special Forces and Local Authorities pension plans.

For Universities Academic, the unfunded liability for service credited prior to January 1, 1992 is being financed by additional contributions of 1.25 per cent of pensionable salaries by the Department, and such percentages by employers and employees as will fund equally the remaining amount as determined by the plan valuation, over the period ending on or before December 31, 2043. Current service costs are funded by employers and employees.

For Special Forces, the unfunded liability for service credited prior to January 1, 1992 is being financed by additional contributions in the ratio of 45.45 per cent by the Department and 27.27 per cent each by employers and employees, over the period ending on or before December 31, 2036. Current service costs are funded by employers and employees. The Act provides that payment of all benefits arising from pensionable service prior to 1994, excluding post-1991 cost of living adjustment benefits, is guaranteed by the Province.

For Local Authorities, the December 31, 1997 actuarial valuation disclosed an actuarial surplus for service credited prior to January 1, 1992. Accordingly, additional contributions by the Province ceased effective January 1, 1998. The obligation reported at March 31, 1998 was eliminated during 1998-99. Current service costs are funded by employers and employees.

Schedule 16

## OTHER ACCRUED LIABILITIES

| | In thousands | |
|---|---|---|
| | 1999 | 1998 |
| Guarantees and indemnities: | | |
| Credit union assistance (a) | $ 98,994 | $ 113,486 |
| Debt of government entities (Schedule 17) | - | 3,800 |
| Other (Schedule 18) | 6,324 | 8,054 |
| Future carrying charges | 3,879 | 8,840 |
| | 109,197 | 134,180 |
| Settlement with Principal Group noteholders | 5,000 | 5,000 |
| Vacation entitlements and long-term disability benefits | 3,273 | 2,730 |
| Deficit of Alberta Risk Management Fund repayable from future appropriations | - | 6,107 |
| Deficiency in N.A. Properties (1994) Ltd. | - | 1,229 |
| | $ 117,470 | $ 149,246 |

(a) The Department has agreed to indemnify and fund interest to the extent necessary on $335,000,000 of debentures issued by S C Financial Ltd. to credit unions in exchange for stabilization preferred shares of the credit unions. The indemnity will expire on October 31, 2010.

Schedule 17

## GUARANTEED DEBT OF GOVERNMENT ENTITIES

| | In thousands | | | | |
|---|---|---|---|---|---|
| | Held by | | | | |
| | Department of Treasury | Alberta Heritage Savings Trust Fund | Others | Total 1999 | Total 1998 |
| Debentures: | | | | | |
| Alberta Municipal Financing Corporation | $ - | $ 140,000 | $ 4,031,761 | $ 4,171,761 | $ 4,403,406 |
| Alberta Social Housing Corporation | 367,053 | 230,558 | 96,117 | 693,728 | 955,703 |
| Alberta Government Telephones Commission | - | - | 200,000 | 200,000 | 400,000 |
| | 367,053 | 370,558 | 4,327,878 | 5,065,489 | 5,759,109 |
| Deposits: | | | | | |
| Alberta Treasury Branches | 86,220 | - | 8,936,090 | 9,022,310 | 8,726,065 |
| Bank Loans and other Liabilities: | | | | | |
| Alberta Social Housing Corporation | | | - | - | 9,401 |
| 475342 Alberta Ltd. | - | - | - | - | 2,852 |
| | - | - | - | - | 12,253 |
| | 453,273 | 370,558 | 13,263,968 | 14,087,799 | 14,497,427 |
| Less: Estimated liability (Schedule 16) | | - | - | - | 3,800 |
| | $ 453,273 | $ 370,558 | $ 13,263,968 | $ 14,087,799 | $ 14,493,627 |

Guarantees include principal borrowings only and exclude guaranteed interest, the amount of which is not determinable.

Schedule 17 (continued)

## GUARANTEED DEBT OF GOVERNMENT ENTITIES (continued)

The net asset positions from the most recent financial statements of government entities with guaranteed liabilities are reported below.

| Entity | Date | Position | 1999 (In thousands) | 1998 (In thousands) |
|---|---|---|---|---|
| Alberta Municipal Financing Corporation | December 31, 1998 | Shareholders' equity | $ 318,666 | $ 333,569 |
| Alberta Social Housing Corporation | March 31, 1999 | Surplus (deficit) | $ 167,656 | $ (68,471) |
| Alberta Government Telephones Commission (a) | December 31, 1998 | Equity | $ 1,064 | $ 977 |
| Alberta Treasury Branches (b) | March 31, 1999 | Equity (deficit) | $ 44,148 | $ (66,544) |

(a) Includes its wholly-owned subsidiary, 475342 Alberta Ltd.

(b) During the year, Alberta Treasury Branches initiated legal actions which resulted in counterclaims aggregating $457,500,000. The eventual outcome of these claims and counterclaims is not determinable.

Schedule 18

## OTHER GUARANTEES (a)

| | 1999 (In thousands) | 1998 (In thousands) | Expiry Date |
|---|---|---|---|
| Farm Credit Stability Act (b) | $ 297,552 | $ 450,470 | 2011 |
| Rural utilities loans | 4,397 | 4,578 | Ongoing |
| Centre for Frontier Engineering Research | 3,055 | 3,380 | 2005 |
| University of Calgary | 1,357 | 1,406 | 2016 |
| Banff Centre for Continuing Education | 1,055 | 1,121 | 2014 |
| Small Business Term Assistance Act | 412 | 662 | (c) |
| Export program | 228 | 230 | (c) |
| Canadian Airlines International Ltd. | - | 11,267 | (c) |
| Pocaterra Development Corporation | - | 1,967 | (c) |
| North Saskatchewan River Boat Ltd. | - | 1,499 | (c) |
| Other under $250,000 | 148 | 120 | (c) |
| | 308,204 | 476,700 | |
| Less: Estimated liability (Schedule 16) | 6,324 | 8,054 | |
| | $ 301,880 | $ 468,646 | |

(a) Authorized loan guarantee limits decline as guaranteed loans are repaid.

The lender takes appropriate security prior to issuing a loan to the borrower which is guaranteed by the Province. The security taken depends on the nature of the loan. Interest rates are negotiated with the lender by the borrower and typically range from prime to prime plus two per cent.

No new program guarantees are being issued under the following Acts or programs: Farm Credit Stability Act, Small Business Term Assistance Act, and Export program. The guarantee program under the Rural Utilities Act is ongoing.

(b) The expiry date shown is the latest expiry date for guaranteed loans under the program.

(c) Loans have expired, are in the process of realization of security, or guarantees are paid out.

ALBERTA HERITAGE FOUNDATION FOR MEDICAL RESEARCH ENDOWMENT FUND
FINANCIAL STATEMENTS
MARCH 31, 1999



## AUDITOR'S REPORT

To the Provincial Treasurer

I have audited the balance sheet of the Alberta Heritage Foundation for Medical Research Endowment Fund as at March 31, 1999 and the statements of income and retained earnings and changes in financial position for the year then ended. These financial statements are the responsibility of the Fund's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In my opinion, these financial statements present fairly, in all material respects, the financial position of the Fund as at March 31, 1999 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles.

Peter Valentine, FCA
Auditor General

Edmonton, Alberta
May 21, 1999

## ALBERTA HERITAGE FOUNDATION FOR MEDICAL RESEARCH ENDOWMENT FUND
## BALANCE SHEET
## MARCH 31, 1999
($ thousands)

| | 1999 | 1998 |
|---|---|---|
| ASSETS | | |
| Portfolio investments (Note 3) | $ 886,783 | $ 797,825 |
| Accrued interest and accounts receivable | - | 6,874 |
| | $ 886,783 | $ 804,699 |
| LIABILITIES, ENDOWMENT AND RETAINED EARNINGS | | |
| Liabilities: | | |
| Payable to the Province of Alberta | $ 20 | $ 44 |
| Endowment (Note 6) | 300,000 | 300,000 |
| Retained earnings (Note 6) | 586,763 | 504,655 |
| | $ 886,783 | $ 804,699 |

The accompanying notes and schedules are part of these financial statements.

## ALBERTA HERITAGE FOUNDATION FOR MEDICAL RESEARCH ENDOWMENT FUND
## STATEMENT OF INCOME AND RETAINED EARNINGS
## FOR THE YEAR ENDED MARCH 31, 1999
($ thousands)

| | 1999 | | 1998 |
|---|---|---|---|
| | Budget | Actual | Actual |
| Income: | | | |
| Investment income (Note 7) | $ 63,000 | $ 118,297 | $ 111,943 |
| Expenses: | | | |
| Transfer to the Alberta Heritage Foundation for Medical Research | 36,000 | 36,000 | 32,000 |
| Administrative expenses (Note 8) | 170 | 189 | 155 |
| | 36,170 | 36,189 | 32,155 |
| Net income | $ 26,830 | 82,108 | 79,788 |
| Retained earnings at beginning of year | | 504,655 | 424,867 |
| Retained earnings at end of year | | $ 586,763 | $ 504,655 |

# ALBERTA HERITAGE FOUNDATION FOR MEDICAL RESEARCH ENDOWMENT FUND
## STATEMENT OF CHANGES IN FINANCIAL POSITION
## FOR THE YEAR ENDED MARCH 31, 1999

($ thousands)

| | 1999 | 1998 |
|---|---|---|
| Operating transactions: | | |
| Net income | $ 82,108 | $ 79,788 |
| Non-cash items included in net income | (58,444) | (19,889) |
| | 23,664 | 59,899 |
| Decrease (increase) in receivables | 6,874 | (2,695) |
| Decrease in payables | (24) | (2,593) |
| Cash provided by operating transactions | 30,514 | 54,611 |
| Investing tranactions: | | |
| Proceeds from disposals, repayments and redemptions of investments | 536,169 | 157,501 |
| Purchase of investments | (563,228) | (235,842) |
| Cash applied to investing transactions | (27,059) | (78,341) |
| Increase (decrease) in cash and cash equivalents | 3,455 | (23,730) |
| Cash and cash equivalents at beginning of year | 17,885 | 41,615 |
| Cash and cash equivalents at end of year | $ 21,340 | $ 17,885 |
| Consisting of Deposit in the Consolidated Cash Investment Trust Fund (Note 3) | $ 21,340 | $ 17,885 |

# ALBERTA HERITAGE FOUNDATION FOR MEDICAL RESEARCH ENDOWMENT FUND
## NOTES TO THE FINANCIAL STATEMENTS
## MARCH 31, 1999

Note 1 Authority and Purpose

The Alberta Heritage Foundation for Medical Research Endowment Fund ("the Fund") operates under the authority of the Alberta Heritage Foundation for Medical Research Act, Chapter A-26, Revised Statutes of Alberta 1980.

The purpose of the Fund is to invest the endowment made to the Fund. The Fund has been managed with the objectives of providing an annual level of income for transfer to the Alberta Heritage Foundation for Medical Research while preserving the capital of the endowment over the long term. The portfolio is comprised of high quality fixed-income securities and equities.

Note 2 Significant Accounting Policies and Reporting Practices

These financial statements are prepared in accordance with generally accepted accounting principles.

The accounting policies of significance to the Fund are as follows:

(a) Portfolio Investments

Fixed-income securities, mortgages and equities held either directly by the Fund or by pooled investment funds are recorded at cost. Cost includes the amount of applicable amortization of discount or premium using the straight-line method over the life of the investments.

The cost of disposals is determined on the average cost basis.

Where there has been a loss in value of an investment that is other than a temporary decline, the investment is written down to recognize the loss. The written down value is deemed to be the new cost.

(b) Income

Investment income is recorded on the accrual basis. Income and expense on index swaps and interest rate swaps are accrued as earned and gains and losses arising as a result of disposals are included in the determination of investment income.

(c) Foreign Currency

Foreign currency transactions are translated into Canadian dollars using average rates of exchange, except for hedged foreign currency transactions which are translated at rates of exchange established by the terms of the forward exchange contracts. Exchange differences on unhedged transactions are included in the determination of investment income.

(d) Investment Valuation

Fair value is the amount of consideration agreed upon in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act. Fair values of investments held either by the Fund or by pooled investment funds are determined as follows:

(i) Public fixed-income securities and equities are valued at the year-end closing sale price, or the average of the latest bid and ask prices quoted by an independent securities valuation company.

(ii) Private fixed-income securities and mortgages are valued based on the net present value of future cash flows. These cash flows are discounted using Government of Canada bond rates adjusted for a risk premium estimated by management.

(iii) The fair value of private equities is estimated by management.

(iv) The fair values of deposits, receivables, accrued interest and payables are estimated to approximate their book values.

(v) The fair value of investments and any other assets and liabilities denominated in a foreign currency are translated at the year-end exchange rate.

## Note 3 Portfolio Investments

Portfolio investments are summarized as follows:

| | 1999 | | | 1998 | | |
|---|---|---|---|---|---|---|
| | Cost | Fair Value | % | Cost | Fair Value | % |
| | | | ($ thousands) | | | |
| Deposit in the Consolidated Cash Investment Trust Fund (a) | $ 21,340 | $ 21,340 | 2.2 | $ 17,885 | $ 17,885 | 1.8 |
| Fixed-income securities: | | | | | | |
| Public, directly held (b) | | | | | | |
| Government of Canada, direct and guaranteed | 2,303 | 2,303 | 0.2 | 220,665 | 262,685 | 27.0 |
| Province of Alberta, guaranteed | - | - | - | 6,588 | 7,272 | 0.8 |
| Other provinces direct and guaranteed | 1,457 | 1,458 | 0.1 | 39,004 | 41,393 | 4.3 |
| Municipal | - | - | - | 4,105 | 4,579 | 0.5 |
| Corporate | - | - | - | 15,296 | 15,317 | 1.6 |
| Canadian Dollar Public Debt Pool (Schedule 1 ) | 338,471 | 335,504 | 34.5 | 36,243 | 36,535 | 3.8 |
| Private Mortgage Pool (c) | 22,397 | 25,853 | 2.7 | 18,786 | 23,629 | 2.4 |
| Floating Rate Note Pool | - | - | - | 34,107 | 34,455 | 3.6 |
| Private Debt Pool | - | - | - | 40,254 | 41,502 | 4.3 |
| Total deposit and fixed-income securities | 385,968 | 386,458 | 39.7 | 432,933 | 485,252 | 50.1 |
| Canadian equities: | | | | | | |
| Canadian Pooled Equity Fund (Schedule 2) | 66,102 | 97,813 | 10.1 | 67,743 | 112,225 | 11.6 |
| Domestic Passive Equity Pooled Fund (Schedule 3) | 107,540 | 125,365 | 12.8 | 22,838 | 23,070 | 2.4 |
| External Managers Fund (Canadian)(Schedule 4) | 42,521 | 42,682 | 4.4 | 18,302 | 23,023 | 2.4 |
| Private Equity Pool (d) | 2,533 | 5,449 | 0.6 | 4,428 | 9,005 | 0.9 |
| Transition Account | - | - | - | 64,398 | 102,290 | 10.6 |
| Foreign equities: | | | | | | |
| External Managers Fund (Global)(Schedule 4) | 105,709 | 122,103 | 12.6 | 94,362 | 107,094 | 11.1 |
| Global Structured Equity Pooled Fund (e) | 106,747 | 107,813 | 11.1 | 54,136 | 55,650 | 5.7 |
| US Passive Equity Pooled Fund (f) | 29,911 | 31,317 | 3.2 | 23,902 | 24,788 | 2.6 |
| External Managers Fund (United States) (Schedule 4) | 17,556 | 31,637 | 3.3 | 13,771 | 23,500 | 2.4 |
| United States Pooled Equity Fund | 573 | 461 | | 1,012 | 1,992 | 0.2 |
| Real Estate: | | | | | | |
| Private Real Estate Pool (g) | 21,623 | 21,638 | 2.2 | - | - | - |
| | 500,815 | 586,278 | 60.3 | 364,892 | 482,637 | 49.9 |
| Total investments | $886,783 | $972,736 | 100.0 | $797,825 | $967,889 | 100.0 |

The majority of the Fund's investments are held in pooled investment funds established and administered by the Provincial Treasurer. Pooled investment funds have a market based unit value that is used to allocate income to participants and to value purchases and sales of pool units. As at March 31, 1999, the Fund's percentage ownership, at market, in pooled investment funds is as follows:

| | % Ownership | |
|---|---|---|
| | 1999 | 1998 |
| Canadian Dollar Public Debt Pool | 4.1 | 0.4 |
| Canadian Pooled Equity Fund | 4.8 | 4.8 |
| Domestic Passive Equity Pooled Fund | 6.2 | 4.3 |
| External Managers Fund | 4.6 | 5.0 |
| Floating Rate Note Pool | - | 2.4 |
| Global Structured Equity Pooled Fund | 7.9 | 5.5 |
| Private Debt Pool | | 5.3 |
| Private Equity Pool | 6.6 | 6.6 |
| Private Mortgage Pool | 2.6 | 3.0 |
| Private Real Estate Pool | 3.0 | |
| Transition Account | - | 6.1 |
| US Passive Equity Pooled Fund | 4.9 | 5.2 |
| United States Pooled Equity Fund | 5.0 | 5.2 |

(a) The Consolidated Cash Investment Trust Fund is managed with the objective of providing competitive interest income to depositors while maintaining maximum security and liquidity of depositors' capital. The portfolio is comprised of high-quality short-term and mid-term fixed-income securities with a maximum term to maturity of five years.

(b) As at March 31, 1999, short-term public fixed-income securities have an average effective yield of 4.80% per annum based on market (1998: 4.88% per annum). At March 31, 1999, securities with a fair value of $2,300,000 (1998: $40,762,000) were loaned to certain borrowers. The loans were secured by marketable securities with a fair value of $2,518,000 (1998: $43,126,000). During the term of the loans, the Fund retains the right to receive income on the investments loaned, in addition to the fee earned.

(c) The Private Mortgage Pool is managed with the objective of providing investment returns higher than attainable from the publicly traded bond market over a five to ten year period. The portfolio is comprised primarily of high quality commercial mortgage loans. Risk is reduced by limiting investments to include only NHA insured loans and first mortgage loans that provide diversification by property usage. The Pool does not invest in mortgages on single family houses, hotels, motels, trailer parks or recreational properties. As at March 31, 1999, mortgages held by the Pool have an average effective yield of 7.08% per annum based on market (1998: 7.37% per annum) and the following term structure based on par: under 1 year - 9%; 1 to 5 years - 33%; 5 to 10 years - 42%; over 10 years - 16%.

(d) The Private Equity Pool is managed with the objective of providing investment returns higher than attainable from the TSE 300 Index over a five to ten year period. The portfolio is comprised of equity investments in companies that show higher than average growth potential. Risk is reduced by avoiding direct investments in start-up and venture capital situations and by limiting holdings in any single company.

(e) The Global Structured Equity Pooled Fund is managed with the objective of providing investment returns comparable to the total return of the Morgan Stanley World Equity Index. The Pool provides exposure to global markets through the use of structured investments such as foreign equity index swaps and as at March 31, 1999, 90% (1998: 81%) of the Pool's underlying investments supporting the index swaps are held in units of the Floating Rate Note Pool [see Schedule 3 (a)].

(f) The US Passive Equity Pooled Fund is a passively managed United States equity fund that provides a return equal to the total return of the Standard & Poor's 500 United States Equity Index. Futures, swaps and other structured investments may be used to enhance performance of the fund.

(g) The Private Real Estate Pool is managed with the objective of providing investment returns comparable to the Russell Canadian Property Index over a five to ten year period. Real Estate is held through intermediate companies which have issued to the pool, common shares and participating debentures secured by a charge on real estate. Risk is reduced by investing in properties that provide diversification by geographic location, by property type and by tenancy. As real estate returns are positively correlated to inflation and negatively correlated to returns from fixed income securities and equities, the pool provides diversification from the securities market with opportunities for high returns.

Note 4 Investment Risk Management

Income and financial returns of the Fund are exposed to credit risk and price risk. Credit risk relates to the possibility that a loss may occur from the failure of another party to perform according to the terms of a contract. Price risk is comprised of currency risk, interest rate risk and market risk. Currency risk relates to the possibility that the investments will change in value due to future fluctuations in foreign exchange rates. Interest rate risk relates to the possibility that the investments will change in value due to future fluctuations in market interest rates. Market risk relates to the possibility that the investments will change in value due to future fluctuations in market prices.

In order to earn an optimal financial return at an acceptable level of risk, management of the Fund has established a policy asset mix of 35% to 65% fixed-income instruments and 35% to 65% equities. Risk is reduced through asset class diversification, diversification within each asset class, quality constraints on fixed-income instruments, and restrictions on amounts exposed to countries designated as emerging markets. Borrowing or leveraging is not allowed with the exception of pre-existing mortgages on real estate properties. Controls are in place respecting the use of derivatives (see Note 5). Forward foreign exchange contracts may be used to manage currency exposure in connection with securities purchased in foreign currency (see Note 5).

Note 5 Index Swaps, Interest Rate Swaps, Foreign Exchange and Futures Contracts

The Fund uses index and interest rate swaps directly, or indirectly through pooled funds to enhance return. A swap is a contractual agreement between two parties to exchange a series of cash flows based on a notional amount and does not involve the exchange of the underlying principal.

An index swap involves the exchange of a floating interest rate cash flow for one based on the performance of a market index. For interest rate swaps, parties generally exchange fixed and floating rate interest cash flows based on a notional value. Notional value is the amount to which a rate or price is applied in order to calculate the exchange of cash flows. All swaps are supported by underlying securities. Leveraging is not allowed.

The following is a summary of the Fund's proportionate share of the notional value of index and interest rate swaps held directly or issued by pooled funds as at March 31, 1999.

| | 1999 | 1998 |
|---|---|---|
| | ($ thousands) | |
| Index swaps: | | |
| Foreign equities (Global Structured Equity Pooled Fund) | $ 105,957 | $ 54,626 |
| Bonds (Canadian Dollar Public Debt Pool) | 62,948 | 6,644 |
| Canadian equities (Domestic Passive Equity Pooled Fund) | 47,928 | 13,481 |
| United States equities (US Passive Equity Pooled Fund) | 30,918 | 23,393 |
| Bonds, directly held | | 23,011 |
| Canadian equities, directly held | | 45,990 |
| Canadian equities (Transition Account) | - | 13,015 |
| Interest rate swaps: | | |
| Global Structured Equity Pooled Fund | 75,456 | 31,336 |
| Canadian Dollar Public Debt Pool | 45,239 | 3,326 |
| Domestic Passive Equity Pooled Fund | 36,418 | 5,636 |
| US Passive Equity Pooled Fund | 2,801 | - |
| Floating Rate Note Pool | - | 24,088 |
| Transition Account | - | 4,290 |
| Total | $ 407,665 | $ 248,836 |

Fair values of swaps have been included in the determination of the fair values of the respective pooled investment funds. Credit exposure relating to swaps is minimal as management deals only with the most credit worthy counterparties.

Foreign exchange contracts are contractual agreements to exchange specified currencies at an agreed upon exchange rate and on an agreed settlement date in the future. As at March 31, 1999, the Fund's proportionate share of outstanding forward foreign exchange contracts issued by the External Managers Fund amounted to $30,223,000 (1998: $19,581,000).

A stock index futures contract is an agreement to take or make delivery of an amount of cash reflecting the difference between changes in the level of the specified stock index. As at March 31, 1999, the Fund's proportionate share of the notional value of stock index futures contracts issued by the External Managers Fund amounted to $1,248,000 (1998: $Nil).

Note 6 Endowment and Retained Earnings

The endowment was received from the Alberta Heritage Savings Trust Fund on March 31, 1980. The Alberta Heritage Foundation for Medical Research Act provides that money required by the Foundation for the furtherance of its objectives shall be paid from the Fund, but no money shall be paid out of the Fund if the payment would result in the value of the assets of the Fund, at cost, being less than the endowment received by the Fund.

As at March 31, 1999, the fair value of endowment and retained earnings amounted to approximately $972,716,000 (1998: $974,719,000).

## Note 7 Investment Income

| | 1999 | 1998 |
|---|---|---|
| | ($ thousands) | |
| **Deposits and fixed-income securities:** | | |
| Deposit in the Consolidated Cash Investment Trust Fund | $ 733 | $ 483 |
| Public fixed-income securities, directly held | | |
| Government of Canada, direct and guaranteed | 45,839 | 19,983 |
| Alberta, direct and guaranteed | 746 | 631 |
| Other provincial, direct and guaranteed | 3,523 | 3,291 |
| Municipal | 484 | 517 |
| Corporate | 754 | 462 |
| Swaps | 288 | 1,879 |
| Security lending | 9 | 35 |
| Canadian Dollar Public Debt Pool | 20,006 | 4,904 |
| Floating Rate Note Pool | 1,699 | 812 |
| Private Debt Pool | 2,461 | 918 |
| Private Mortgage Pool | 3,517 | 1,948 |
| | 80,059 | 35,863 |
| **Equities:** | | |
| Canadian Pooled Equity Fund | 4,449 | 12,987 |
| Transition Account | 1,561 | 4,015 |
| Domestic Passive Equity Pooled Fund | 5,217 | 3,539 |
| External Managers Fund (Canadian) | 209 | 968 |
| Private Equity Pool | 773 | 1,410 |
| External Managers Fund (Global) | 10,977 | 7,667 |
| Global Structured Equity Pooled Fund | 12,611 | 13,697 |
| United States Pooled Equity Fund | 464 | 18,087 |
| US Passive Equity Pooled Fund | 5,919 | 277 |
| External Managers Fund (United States) | 3,342 | 3,418 |
| Swaps | (7,575) | 10,015 |
| Private Real Estate Pool | 291 | - |
| | 38,238 | 76,080 |
| Investment income | $ 118,297 | $ 111,943 |

Investment income is comprised of interest, dividends, amortization of discount or premium, swap income, security lending income and realized gains and losses, net of write-downs on investments. The Fund's share of income earned from pooled investment funds is net of administrative expenses incurred by the pool (see Note 8).

Investment income includes net gains from disposal of investments totalling $75,529,000 (1998: $44,494,000).

## Note 8 Administrative Expenses

Administrative expenses include investment management, cash management and safekeeping costs charged on a cost-recovery basis directly by the Department of Treasury. External management and custodial fees are deducted directly from investment income of the External Managers Fund (Canadian, Global and United States). During the year, the Fund's share of administrative expenses deducted directly from investment income of externally and internally managed pooled funds (see Note 7) amounted to $727,000 and $108,000 respectively (1998: $620,000 and $59,000). Total administrative expense during the year, including amounts deducted directly from investment income of pooled funds, amounted to $1,024,000 (1998: $834,000).

## Note 9 Uncertainty Due to the Year 2000

The year 2000 issue is the result of some computer systems using two digits rather than four to define the applicable year. Government computer systems that have date sensitive software may recognize a date using "00" as the year 1900 rather than the year 2000, which could result in miscalculations or system failures. In addition, similar problems may arise in some systems if certain dates in 1999 are not recognized as a valid date or are recognized to represent something other than a date. The effects of the year 2000 issue may be experienced before, on, or after January 1, 2000. If not addressed, the effect on operations and financial reporting may range from minor errors to significant systems failure that could affect the ability to conduct some government operations. Despite the government's efforts to address this issue, it is not possible to be certain that all aspects of the year 2000 issue affecting the Fund, including those related to the efforts of customers, suppliers and other third parties, will be fully resolved.

Note 10 Comparative Figures

Certain 1998 figures have been reclassified to conform to 1999 presentation.

Note 11 Approval of Financial Statements

These financial statements were approved by management.

Schedule 1

# ALBERTA HERITAGE FOUNDATION FOR MEDICAL RESEARCH ENDOWMENT FUND SCHEDULE OF INVESTMENTS IN CANADIAN DOLLAR PUBLIC DEBT POOL MARCH 31, 1999

($ thousands)

| | 1999 | | 1998 | |
|---|---|---|---|---|
| | Cost | Fair Value | Cost | Fair Value |
| Deposit in the Consolidated Cash Investment Trust Fund | $ 4,727 | $ 4,727 | $ 467 | $ 467 |
| Public fixed-income securities (b) | | | | |
| Government of Canada direct and guaranteed | 91,264 | 92,246 | 12,252 | 12,588 |
| Provincial: | | | | |
| Alberta, direct and guaranteed | 7,710 | 7,992 | 982 | 1,045 |
| Other, direct and guaranteed | 42,226 | 43,757 | 5,866 | 6,074 |
| Municipal | 3,444 | 3,428 | 299 | 312 |
| Corporate | 136,450 | 132,776 | 16,037 | 15,709 |
| Private fixed-income securities | | | | |
| Corporate | 48,607 | 46,535 | - | - |
| | 334,428 | 331,461 | 35,903 | 36,195 |
| Accrued interest and accounts receivable | 8,172 | 8,172 | 625 | 625 |
| Accounts payable | (4,129) | (4,129) | (285) | (285) |
| | 4,043 | 4,043 | 340 | 340 |
| Total - Alberta Heritage Foundation for Medical Research Endowment Fund | $ 338,471 | $ 335,504 | $ 36,243 | $ 36,535 |
| Total - Canadian Dollar Public Debt Pool (a) | $ 7,812,035 | $ 8,112,618 | $ 6,635,228 | $ 7,000,911 |

(a) The Canadian Dollar Public Debt Pool is managed with the objective of providing above average returns compared to the total return of the Scotia Capital Market Universe Bond Index over a four-year period while maintaining adequate security and liquidity of participants' capital. The portfolio is comprised of high quality Canadian fixed income instruments and debt related derivatives. Competitive returns are achieved through management of the portfolio duration and sector rotation.

(b) As at March 31, 1999, securities held by the pool have an average effective yield of 5.51% per annum based on market (1998: 5.41% per annum) and the following term structure based on par: under 1 year - 10%; 1 to 5 years - 37%; 5 to 10 years - 24%; 10 to 20 years - 21%; over 20 years - 8%.

Schedule 2

# ALBERTA HERITAGE FOUNDATION FOR MEDICAL RESEARCH ENDOWMENT FUND
## SCHEDULE OF INVESTMENTS IN CANADIAN POOLED EQUITY FUND
## MARCH 31, 1999

($ thousands)

| | 1999 | | 1998 | |
|---|---|---|---|---|
| | Cost | Fair Value | Cost | Fair Value |
| Deposit in the Consolidated Cash Investment Trust Fund | $ 580 | $ 580 | $ 3,746 | $ 3,746 |
| Canadian public equities (b): | | | | |
| Common shares and rights: | | | | |
| Communications and media | 3,469 | 6,665 | 1,232 | 2,746 |
| Conglomerates | 3,325 | 5,477 | 3,512 | 6,769 |
| Consumer products | 3,245 | 4,708 | 2,263 | 3,692 |
| Financial services | 12,789 | 20,841 | 10,813 | 22,956 |
| Gold and precious minerals | 4,080 | 4,272 | 3,741 | 4,928 |
| Industrial products | 12,225 | 20,067 | 8,411 | 16,661 |
| Merchandising | 1,665 | 2,411 | 1,773 | 3,084 |
| Metals and minerals | 3,313 | 3,192 | 4,707 | 5,370 |
| Oil and gas | 6,692 | 7,340 | 13,658 | 16,632 |
| Paper and forest products | 1,739 | 1,956 | 2,256 | 3,126 |
| Pipelines | 1,878 | 2,552 | 1,526 | 2,807 |
| Real estate and construction | 2,082 | 2,356 | 1,468 | 1,995 |
| Transportation and environmental services | 2,143 | 2,465 | 2,645 | 5,107 |
| Utilities | 6,084 | 11,854 | 4,987 | 11,344 |
| Passive index | 1,002 | 1,286 | 733 | 990 |
| | 65,731 | 97,442 | 63,725 | 108,207 |
| Accrued interest and accounts receivable | 608 | 608 | 272 | 272 |
| Accounts payable | (817) | (817) | - | - |
| | (209) | (209) | 272 | 272 |
| Total - Alberta Heritage Foundation for Medical Research Endowment Fund | $ 66,102 | $ 97,813 | $ 67,743 | $ 112,225 |
| Total - Canadian Pooled Equity Fund (a) | $ 1,788,730 | $ 2,045,408 | $ 1,841,419 | $ 2,327,728 |

(a) The Canadian Pooled Equity Fund is managed with the objective of providing competitive returns comparable to the total return of the Toronto Stock Exchange 300 Index. The portfolio is comprised of publicly traded equities in Canadian corporations. Risk is reduced by prudent security selection and sector rotation.

(b) The industrial classifications are those used by the Toronto Stock Exchange.

Schedule 3

# ALBERTA HERITAGE FOUNDATION FOR MEDICAL RESEARCH ENDOWMENT FUND
## SCHEDULE OF INVESTMENTS IN DOMESTIC PASSIVE EQUITY POOLED FUND
## MARCH 31, 1999

($ thousands)

| | 1999 | | 1998 | |
|---|---|---|---|---|
| | Cost | Fair Value | Cost | Fair Value |
| Deposit in the Consolidated Cash Investment Trust Fund | $ 423 | $ 423 | $ 272 | $ 272 |
| Fixed-income securities, corporate | 693 | 799 | 847 | 779 |
| Floating Rate Note Pool | 35,304 | 40,683 | 5,131 | 4,738 |
| | 36,420 | 41,905 | 6,250 | 5,789 |
| Canadian public equities (b): | | | | |
| Common shares and rights: | | | | |
| Communications and media | 4,136 | 6,388 | 510 | 622 |
| Conglomerates | 2,042 | 2,374 | 282 | 362 |
| Consumer products | 2,745 | 3,441 | 525 | 549 |
| Financial services | 10,638 | 14,555 | 1,314 | 2,029 |
| Gold and precious minerals | 4,687 | 3,349 | 966 | 596 |
| Industrial products | 11,387 | 14,915 | 1,444 | 1,806 |
| Merchandising | 2,527 | 3,011 | 395 | 464 |
| Metals and minerals | 3,513 | 2,479 | 561 | 409 |
| Oil and gas | 8,435 | 7,090 | 1,394 | 1,333 |
| Paper and forest products | 2,318 | 2,227 | 410 | 370 |
| Pipelines | 1,765 | 1,948 | 141 | 199 |
| Real estate and construction | 1,707 | 1,661 | 189 | 213 |
| Transportation and environmental services | 1,598 | 1,577 | 219 | 288 |
| Utilities | 5,478 | 9,140 | 707 | 1,049 |
| Passive index | 1,093 | 1,263 | 233 | 246 |
| | 64,069 | 75,418 | 9,290 | 10,535 |
| Domestic Structured Equity Pooled Fund | 6,726 | 7,699 | 6,485 | 5,933 |
| United States Public Equities | 122 | 140 | - | - |
| Accrued interest and accounts receivable | 407 | 407 | 844 | 844 |
| Accounts payable | (204) | (204) | (31) | (31) |
| | 203 | 203 | 813 | 813 |
| Total - Alberta Heritage Foundation for Medical Research Endowment Fund | $ 107,540 | $ 125,365 | $ 22,838 | $ 23,070 |
| Total - Domestic Passive Equity Pooled Fund (a) | $ 1,983,918 | $ 2,005,862 | $ 493,372 | $ 539,403 |

(a) The Domestic Passive Equity Pooled Fund is managed on a passive approach with the objective of providing investment returns comparable to the Toronto Stock Exchange (TSE) 300 Index. The portfolio is comprised of publicly traded equities in Canadian corporations similar in weights to the TSE 300 Index. To enhance investment returns with no substantial increase in risks, the pooled fund invests in the Domestic Structured Equity Pooled Fund (DSEP) and the Floating Rate Note Pool (FRNP) which are pooled investment funds established and administered by the Provincial Treasurer. DSEP provides exposure to the Canadian equity markets through the use of structured investments such as index swaps and interest rate swaps. It provides returns comparable to the TSE indices. FRNP is managed with the objective of generating floating rate income needed for the swap obligations of the participants with structured investments in equities and bonds. Through the use of structured investments such as interest rate swaps, FRNP provides investment opportunities in high quality floating rate instruments with remaining term-to-maturity of ten years or less.

(b) The industrial classifications are those used by the Toronto Stock Exchange.

Schedule 4

# ALBERTA HERITAGE FOUNDATION FOR MEDICAL RESEARCH ENDOWMENT FUND
# SCHEDULE OF INVESTMENTS IN EXTERNAL MANAGERS FUND
# MARCH 31, 1999

($ thousands)

| | 1999 | | 1998 | |
|---|---|---|---|---|
| | Cost | Fair Value | Cost | Fair Value |
| Foreign Public Equity Pools | | | | |
| Multi-region | $ 46,226 | $ 53,884 | $ 41,521 | $ 49,170 |
| Europe | 34,725 | 39,770 | 27,837 | 37,680 |
| Pacific basin | 22,951 | 25,904 | 25,004 | 20,244 |
| Emerging markets | 1,807 | 2,545 | - | - |
| | 105,709 | 122,103 | 94,362 | 107,094 |
| United States | 17,556 | 31,637 | 13,771 | 23,500 |
| Canadian Public Equity Pools | | | | |
| Large Capitalized companies | 24,586 | 24,032 | - | - |
| Small Capitalized companies | 17,935 | 18,650 | 18,302 | 23,023 |
| | 42,521 | 42,682 | 18,302 | 23,023 |
| Total - Alberta Heritage Foundation for Medical Research Endowment Fund | $ 165,786 | $ 196,422 | $ 126,435 | $ 153,617 |
| Total - External Managers Fund (a)(b) | $ 3,537,968 | $ 4,338,781 | $ 2,399,553 | $ 3,043,960 |

(a) The Fund is managed by external managers with expertise in global equity markets and Canadian small capitalized companies and large capitalized companies. The objective of the Fund is to provide investment returns higher than the total return of the applicable Morgan Stanley, Standard and Poor's and Toronto Stock Exchange indices over a four year period. The portfolio is comprised of publicly traded equity securities on Canadian and approved foreign markets. Risk is reduced through manager, style and market diversification.

(b) The following is a summary of assets and liabilities of the External Managers Fund as at March 31, 1999.

| | 1999 | 1998 |
|---|---|---|
| | ($ thousands) | |
| Cash and short-term securities | $ 109,079 | $ 130,426 |
| Investments | | |
| Public equities | 3,438,393 | 2,270,812 |
| Fixed income securities | 1,247 | 3,936 |
| Accrued interest and accounts receivable | 27,890 | 27,357 |
| Accounts payable | (38,641) | (32,978) |
| Total - External Managers Fund | $ 3,537,968 | $ 2,399,553 |

ALBERTA HERITAGE SAVINGS TRUST FUND
FINANCIAL STATEMENTS
MARCH 31, 1999



## AUDITOR'S REPORT

To the Provincial Treasurer

I have audited the balance sheet of the Alberta Heritage Savings Trust Fund as at March 31, 1999 and the statements of operations and changes in financial position for the year then ended. These financial statements are the responsibility of the Fund's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In my opinion, these financial statements present fairly, in all material respects, the financial position of the Fund as at March 31, 1999 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles.

Peter Valentine, FCA
Auditor General

Edmonton, Alberta
May 21, 1999

## ALBERTA HERITAGE SAVINGS TRUST FUND
## BALANCE SHEET
## MARCH 31, 1999
($ thousands)

| | 1999 | 1998 |
|---|---|---|
| **ASSETS** | | |
| Portfolio investments: | | |
| Endowment portfolio (Schedule 1) | $ 3,906,359 | $ 2,764,586 |
| Transition portfolio (Schedule 2) | 8,053,014 | 9,369,888 |
| Accrued interest and accounts receivable | 138,153 | 174,792 |
| | $ 12,097,526 | $ 12,309,266 |
| **LIABILITIES AND FUND EQUITY** | | |
| Liabilities: | | |
| Accounts payable | $ 3,195 | $ 84,601 |
| Due to the General Revenue Fund | 68,012 | 198,346 |
| | 71,207 | 282,947 |
| Fund equity (Note 5): | | |
| Endowment portfolio | 3,818,649 | 2,613,202 |
| Transition portfolio | 8,207,670 | 9,413,117 |
| | 12,026,319 | 12,026,319 |
| | $ 12,097,526 | $ 12,309,266 |

The accompanying notes and schedules are part of these financial statements.

## ALBERTA HERITAGE SAVINGS TRUST FUND
## STATEMENT OF OPERATIONS
## FOR THE YEAR ENDED MARCH 31, 1999
($ thousands)

| | 1999 | | 1998 |
|---|---|---|---|
| | Budget | Actual | Actual |
| Income: | | | |
| Investment income: | | | |
| Endowment portfolio | $ 189,000 | $ 270,545 | $ 293,898 |
| Transition portfolio | 614,400 | 663,117 | 769,585 |
| | 803,400 | 933,662 | 1,063,483 |
| Expenses: | | | |
| Administrative expenses (Note 7) | 2,200 | 1,651 | 1,956 |
| Provision for loan impairment in the Transition portfolio | - | - | 114,219 |
| | 2,200 | 1,651 | 116,175 |
| Net income (Note 6) | 801,200 | 932,011 | 947,308 |
| Transfers: | | | |
| Transfers to the General Revenue Fund | 716,200 | 932,011 | 922,347 |
| Amounts retained (Note 5) | 85,000 | - | 24,961 |
| Net increase in fund equity | $ 85,000 | - | 24,961 |
| Fund equity at beginning of year | | 12,026,319 | 12,001,358 |
| Fund equity at end of year | | $ 12,026,319 | $ 12,026,319 |

## ALBERTA HERITAGE SAVINGS TRUST FUND
## STATEMENT OF CHANGES IN FINANCIAL POSITION
## FOR THE YEAR ENDED MARCH 31, 1999

($ thousands)

| | 1999 | 1998 |
|---|---|---|
| Operating transactions: | | |
| Net income | $ 932,011 | $ 947,308 |
| Non-cash items included in net income | (82,755) | 20,595 |
| | 849,256 | 967,903 |
| Decrease in receivables | 36,639 | 83,150 |
| Increase (decrease) in payables | (81,406) | 49,561 |
| Cash provided by operating transactions | 804,489 | 1,100,614 |
| Investing transactions: | | |
| Proceeds from disposals, repayments and redemptions of investments | 7,817,615 | 13,520,333 |
| Purchase of investments | (7,603,587) | (13,777,554) |
| Cash provided by (applied to) investing transactions | 214,028 | (257,221) |
| Transfers: | | |
| Transfers to the General Revenue Fund | (932,011) | (922,347) |
| Increase (decrease) in Due to the General Revenue Fund | (130,334) | 150,898 |
| Cash applied to transfers | (1,062,345) | (771,449) |
| Increase (decrease) in cash and cash equivalents | (43,828) | 71,944 |
| Cash and cash equivalents at beginning of year | 211,342 | 139,398 |
| Cash and cash equivalents at end of year | $ 167,514 | $ 211,342 |
| Consisting of Deposits in the Consolidated Cash Investment Trust Fund: | | |
| Endowment Portfolio (Schedule 1) | $ 122,504 | $ 132,730 |
| Transition Portfolio (Schedule 2) | 45,010 | 78,612 |
| | $ 167,514 | $ 211,342 |

## ALBERTA HERITAGE SAVINGS TRUST FUND
## NOTES TO THE FINANCIAL STATEMENTS
## MARCH 31, 1999

Note 1 Authority and Mission

The Alberta Heritage Savings Trust Fund operates under the authority of the Alberta Heritage Savings Trust Fund Act (the Act), Chapter A-27.01, Revised Statutes of Alberta 1980, as amended.

The preamble to the Act describes the mission of the Fund as follows:

*"To provide prudent stewardship of the savings from Alberta's non-renewable resources by providing the greatest financial returns on those savings for current and future generations of Albertans."*

Investments of the Fund are held in an Endowment Portfolio and a Transition Portfolio. The Endowment Portfolio has the objective of maximizing long-term financial returns. The Transition Portfolio has the objective of providing income support to the Government's consolidated fiscal plan over the short term to medium term. Commencing in 1996-97, the Act provides that all assets in the Transition Portfolio must be transferred to the Endowment Portfolio by December 31, 2005.

Note 2 Summary of Significant Accounting Policies and Reporting Practices

These financial statements are prepared in accordance with generally accepted accounting principles.

The accounting policies of significance to the Fund are as follows:

(a) Portfolio investments

Fixed-income securities, mortgages, equities, and real estate investments held directly by the Fund or by pooled investment funds are recorded at cost. Cost includes the amount of applicable amortization of discount or premium using the straight-line method over the life of the investments.

Investments in loans are recorded at cost less any unearned income and allowance for credit loss. Where there is no longer reasonable assurance of timely collection of the full amount of principal and interest of a loan, a specific provision for credit loss is made and the carrying amount of the loan is reduced to its estimated realizable amount.

The cost of disposals is determined on the average cost basis.

Where there has been a loss in value of an investment in fixed-income securities, mortgages, equities and real estate that is other than a temporary decline, the investment is written down to recognize the loss. The written down value is deemed to be the new cost.

(b) Investment Income

Investment income is recorded on the accrual basis where there is reasonable assurance as to its measurement and collectability. When a loan becomes impaired, recognition of interest income in accordance with the terms of the original loan agreement ceases. Any subsequent payments received on an impaired loan are applied to reduce the loan's book value.

Income and expense on index swaps and interest rate swaps are accrued as earned and gains and losses arising as a result of disposal of investments are included in the determination of investment income.

(c) Foreign Currency

Foreign currency transactions are translated into Canadian dollars using average rates of exchange, except for hedged foreign currency transactions which are translated at rates of exchange established by the terms of the forward exchange contracts. Exchange differences on unhedged transactions are included in the determination of investment income.

(d) Investment Valuation

Fair value is the amount of consideration agreed upon in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act. Fair values of investments held either directly by the Fund or by pooled investment funds are determined as follows:

(i) Public fixed-income securities and equities are valued at the year-end closing sale price, or the average of the latest bid and ask prices quoted by an independent securities valuation company.

(ii) Private fixed income securities, mortgages, provincial debentures are valued based on the net present value of future cash flows. These cash flows are discounted using appropriate interest rate premiums over similar Government of Canada benchmark bonds trading in the market.

(iii) The fair value of private equities is estimated by management.

(iv) Real estate investments are reported at their most recent appraised value, net of any liabilities against the real property. Real estate properties are appraised annually by qualified external real estate appraisers.

(v) Fair value of loans are not reported due to there being no organized financial market for the instruments and it is not practicable within constraints of timeliness or cost to estimate the fair values with sufficient reliability.

(vi) The fair value of deposits, receivables, accrued interest and payables are estimated to approximate their book values.

(vii) The fair value of investments and any other assets and liabilities denominated in a foreign currency are translated at the year-end exchange rate.

## Note 3 Investment Risk Management

Income and financial returns of the Fund are exposed to credit risk and price risk. Credit risk relates to the possibility that a loss may occur from the failure of another party to perform according to the terms of a contract. Price risk is comprised of currency risk, interest rate risk and market risk. Currency risk relates to the possibility that the investments will change in value due to future fluctuations in foreign exchange rates. Interest rate risk relates to the possibility that the investments will change in value due to future fluctuations in market interest rates. Market risk relates to the possibility that the investments will change in value due to future fluctuations in market prices.

The *Standing Committee on the Alberta Heritage Savings Trust Fund* reviews and approves the business plan of the Fund. In order to earn an optimal financial return at an acceptable level of risk, the 1998-99 business plan establishes an asset mix policy of 35% to 55% fixed-income instruments and 45% to 65% equities for the Endowment Portfolio and limits investments of the Transition Portfolio to include only fixed-income securities other than securities transferred from the old structure. Risk is reduced through asset class diversification, diversification within each asset class, quality and duration constraints on fixed-income instruments, and restrictions on amounts exposed to countries designated as emerging markets. Borrowing or leveraging is not allowed with the exception of pre-existing mortgages on real estate. Controls are in place respecting the use of derivatives (see Note 4). Forward foreign exchange contracts may be used to manage currency exposure in connection with securities purchased in foreign currency (see Note 4).

## Note 4 Index Swaps, Interest Rate Swaps, Foreign Exchange and Futures Contracts

The Fund uses index and interest rate swaps held directly, or indirectly through pooled funds, to enhance return and for hedging risks. A swap is a contractual agreement between two parties to exchange a series of cash flows based on a notional amount and does not involve the exchange of the underlying principal.

An index swap involves the exchange of a floating interest rate cash flow for one based on the performance of a market index. For interest rate swaps, parties generally exchange fixed and floating rate interest cash flows based on a notional value. The notional value is the amount to which a rate is applied in order to calculate the exchange of cash flows. All swaps are supported by underlying securities. Leveraging is not allowed.

The following is a summary of the Fund's proportionate share of the notional amount of index swaps and interest rate swaps held directly or issued by pooled funds at March 31, 1999:

| | 1999 | 1998 |
|---|---|---|
| | ($ thousands) | |
| Index swaps: | | |
| Bonds (Canadian Dollar Public Debt Pool) | $ 250,319 | $ 153,783 |
| Canadian equities, directly held | 142,069 | 159,924 |
| Foreign equities (Global Structured Equity Pooled Fund) | 292,227 | 163,946 |
| United States equities (US Passive Equity Pooled Fund) | 168,296 | 59,523 |
| Interest rate swaps: | | |
| Directly held | 134,614 | 65,000 |
| Canadian Dollar Public Debt Pool | 179,896 | 76,977 |
| Global Structured Equity Pooled Fund | 208,107 | 94,047 |
| Floating Rate Note Pool | 138,048 | 108,365 |
| US Passive Equity Pooled Fund | 15,247 | |
| Total | $ 1,528,823 | $ 881,565 |

The fair value of swaps have been included in the determination of the fair value of the respective pooled investment funds.

Foreign exchange contracts are contractual agreements to exchange specified currencies at an agreed upon exchange rate and on an agreed settlement date in the future. As at March 31, 1999, the Fund's proportionate share of outstanding forward foreign exchange contracts issued by the External Managers Fund amounted to $145,486,000 (1998: $67,768,000).

A stock index futures contract is an agreement to take or make delivery of an amount of cash reflecting the difference between changes in the level of the specified stock index. As at March 31, 1999, the Fund's proportionate share of the notional value of stock index futures contracts issued by the External Managers Fund amounted to $5,062,000 (1998: $Nil).

## Note 5 Fund Equity

Each year, commencing in 1996-97, a minimum of $1.2 billion of assets, at cost, will be transferred to the Endowment Fund from the Transition Fund until all assets are transferred no later than 2005. In 1998-99 the Lieutenant Governor in Council approved this transfer of assets with a book value of not less than $1.2 billion.

Annually, a portion of net income of the Fund was retained in the Endowment Portfolio, as determined by multiplying the net assets of the Fund by the percentage increase in the Canadian gross domestic product price index for the fiscal year. Section 11(1) of the *Alberta Heritage Savings Trust Fund Act (the Act)* required that, until the completion of the 1998-99 fiscal year, the Fund would be allowed to keep the lesser of (i) the income necessary to fully offset inflation, and (ii) the amount, if any, by which the province's surplus exceeds $500 million in that year. On March 23, 1999 the *Fiscal Responsibility Act* received Royal Assent and Section 11(1) of the Act was repealed. Section 11(5) was added to the Act and states that for fiscal years subsequent to 1999 and until the accumulated debt is eliminated, the Provincial Treasurer is not required to retain amounts for inflation proofing in the Fund, but may retain such amounts as the Provincial Treasurer considers advisable. In 1998-99, no portion of the net income of the Fund was retained in the Endowment Portfolio.

Note 6 Net Income

| | Endowment Portfolio | Transition Portfolio | 1999 | 1998 |
|---|---|---|---|---|
| | ($ thousands) | | | |
| Deposit and fixed-income securities: | | | | |
| Deposits in the Consolidated Cash Investment Trust Fund | $ 5,763 | $ 3,168 | $ 8,931 | $ 7,565 |
| Public fixed-income securities, directly held: | | | | |
| Government of Canada, direct and guaranteed | 5,764 | 163,086 | 168,850 | 273,479 |
| Alberta, direct and guaranteed | 1,120 | 11,524 | 12,644 | 15,998 |
| Other provincial, direct and guaranteed | 7,156 | 166,389 | 173,545 | 186,606 |
| Municipal | | 4,336 | 4,336 | 2,696 |
| Corporate | 824 | 179,918 | 180,742 | 146,533 |
| Security lending | 24 | 373 | 397 | 431 |
| Provincial corporation debentures | - | 103,388 | 103,388 | 160,322 |
| Canadian Dollar Public Debt Pool | 87,826 | - | 87,826 | 67,112 |
| Floating Rate Note Pool | 8,318 | - | 8,318 | 3,320 |
| Private Mortgage Pool | 16,406 | - | 16,406 | 7,820 |
| Private Debt Pool | 4,707 | - | 4,707 | 1,889 |
| | 137,908 | 632,182 | 770,090 | 873,771 |
| Equities: | | | | |
| Public Canadian equities, directly held | 22,258 | 30,935 | 53,193 | 75,164 |
| Canadian Pooled Equity Fund | 598 | - | 598 | |
| External Managers Fund (Canadian) | 3,335 | | 3,335 | 2,518 |
| Private Equity Pool | 808 | - | 808 | 1,847 |
| Private Equity Pool (98) | (14) | - | (14) | |
| External Managers Fund (Global) | 44,474 | - | 44,474 | 14,084 |
| Global Structured Equity Pooled Fund | 36,382 | - | 36,382 | 34,205 |
| United States Pooled Equity Fund | 831 | - | 831 | 4,375 |
| US Passive Equity Pooled Fund | 28,038 | - | 28,038 | 658 |
| External Managers Fund (United States) | 16,051 | - | 16,051 | 5,000 |
| Security lending | 82 | | 82 | 44 |
| Swaps, direct | (24,584) | | (24,584) | 50,924 |
| Private Real Estate Pool | 4,378 | - | 4,378 | 893 |
| | 132,637 | 30,935 | 163,572 | 189,712 |
| Investment income | 270,545 | 663,117 | 933,662 | 1,063,483 |
| Administrative expenses (Note 7) | (502) | (1,149) | (1,651) | (1,956) |
| Provision for loan impairment | - | - | - | (114,219) |
| Net Income | $ 270,043 | $ 661,968 | $ 932,011 | $ 947,308 |

Investment income is comprised of interest, dividends, amortization of discount and premiums, swap income, security lending income and realized gains and losses, net of write-downs, on investments.

Investment income from the Endowment portfolio and the Transition portfolio includes net gains from disposal of investments totalling $83,614,000 (1998: $101,081,000) and $70,774,000 (1998: $91,427,000) respectively.

Note 7 Administrative Expenses

Administrative expenses includes investment management, cash management, safekeeping costs and other expenses charged on a cost-recovery basis directly from the Department of Treasury. External management and custodial fees are deducted directly from investment income of External Managers Fund (Canadian, Global and United States). During the year, the Fund's share of administrative expenses deducted directly from investment income of externally and internally managed pooled funds (see Note 6) amounted to $2,896,000 and $493,000 respectively (1998: $1,381,000 and $161,000). Total administrative expense during the year, including amounts deducted directly from investment income of pooled funds, amounted to $5,040,000 (1998: $3,498,000) or approximately 4 basis points on rate of return (1998: 3 basis points).

Note 8 Uncertainty Due to the Year 2000

The year 2000 issue is the result of some computer systems using two digits rather than four to define the applicable year. Government computer systems that have date sensitive software may recognize a date using "00" as the year 1900 rather than the year 2000, which could result in miscalculations or system failures. In addition, similar problems may arise in some systems if certain dates in 1999 are not recognized as a valid date or are recognized to represent something other than a date. The effects of the year 2000 issue may be experienced before, on, or after January 1, 2000. If not addressed, the effect on operations and financial reporting may range from minor errors to significant systems failure that could affect the ability to conduct some government operations. Despite the government's efforts to address this issue, it is not possible to be certain that all aspects of the year 2000 issue affecting the Fund, including those related to the efforts of customers, suppliers and other third parties, will be fully resolved.

Note 9 Comparative Figures

Certain 1998 figures have been reclassified to conform to 1999 presentation.

Note 10 Approval of Financial Statements

These financial statements were approved by management.

Schedule 1

# ALBERTA HERITAGE SAVINGS TRUST FUND
## SCHEDULE OF ENDOWMENT PORTFOLIO INVESTMENTS
## MARCH 31, 1999
($ thousands)

| | 1999 | | | 1998 | | |
|---|---|---|---|---|---|---|
| | Cost | Fair Value | % | Cost | Fair Value | % |
| Deposit in the Consolidated Cash Investment Trust Fund (a) | $ 122,504 | $ 122,504 | 2.8 | $ 132,730 | $ 132,730 | 4.1 |
| Fixed-income securities: | | | | | | |
| Public, directly held (b) | | | | | | |
| Government of Canada, direct and guaranteed | 63,772 | 65,439 | 1.5 | 170,738 | 172,125 | 5.3 |
| Provincial: | | | | | | |
| Alberta, direct | - | - | - | 35,907 | 36,890 | 1.1 |
| Other, direct and guaranteed | 44,830 | 46,059 | 1.1 | 97,850 | 102,060 | 3.1 |
| Corporate | - | - | - | 40,966 | 41,773 | 1.3 |
| Canadian Dollar Public Debt Pool (c ) | 1,350,689 | 1,334,164 | 30.8 | 848,113 | 845,622 | 25.9 |
| Floating Rate Note Pool (d) | 181,982 | 182,865 | 4.2 | 154,509 | 154,998 | 4.7 |
| Private Mortgage Pool (e) | 275,243 | 274,250 | 6.3 | 141,627 | 141,962 | 4.3 |
| Private Debt Pool | - | - | - | 134,587 | 135,338 | 4.1 |
| Total deposit and fixed-income securities (m) | 2,039,020 | 2,025,281 | 46.7 | 1,757,027 | 1,763,498 | 53.9 |
| Canadian equities: | | | | | | |
| Public, directly held (f) | 279,726 | 651,008 | 15.0 | 277,989 | 725,845 | 22.3 |
| Canadian Pooled Equity Fund (g) | 40,598 | 41,760 | 1.0 | - | - | - |
| External Managers Fund (Canadian) (h) | 210,681 | 215,144 | 5.0 | 46,846 | 52,664 | 1.6 |
| Private Equity Pool (i) | 14,177 | 11,273 | 0.3 | 18,614 | 18,356 | 0.6 |
| Private Equity Pool (98) (i) | 14,502 | 14,502 | 0.3 | - | - | - |
| Total Canadian equities (m) | 559,684 | 933,687 | 21.6 | 343,449 | 796,865 | 24.5 |
| Foreign equities: | | | | | | |
| External Managers Fund (Global) (h) | 525,561 | 564,157 | 13.0 | 320,368 | 344,962 | 10.6 |
| Global Structured Equity Pooled Fund (j) | 303,261 | 297,346 | 6.9 | 171,879 | 167,020 | 5.1 |
| US Passive Equity Pooled Fund (k) | 170,381 | 170,466 | 3.9 | 60,823 | 63,073 | 1.9 |
| External Managers Fund (United States) (h) | 143,616 | 171,535 | 4.0 | 72,737 | 84,832 | 2.6 |
| United States Pooled Equity Fund | 3,139 | 1,675 | - | 3,373 | 5,224 | 0.2 |
| Total foreign equities | 1,145,958 | 1,205,179 | 27.8 | 629,180 | 665,111 | 20.4 |
| Real estate (l) | 161,697 | 170,146 | 3.9 | 34,930 | 39,234 | 1.2 |
| Total equities and real estate (m) | 1,867,339 | 2,309,012 | 53.3 | 1,007,559 | 1,501,210 | 46.1 |
| Total investments (n) | $ 3,906,359 | $ 4,334,293 | 100.0 | $ 2,764,586 | $ 3,264,708 | 100.0 |

The majority of the Endowment portfolio investments are held in pooled investment funds established and administered by the Provincial Treasurer. Pooled investment funds have a market based unit value that is used to allocate income to participants and to value purchases and sales of pool units. As at March 31, 1999, the Fund's percentage ownership, at market, in pooled investment funds is as follows:

| | % Ownership | |
|---|---|---|
| | 1999 | 1998 |
| Canadian Dollar Public Debt Pool | 16.4 | 12.1 |
| Canadian Pooled Equity Fund | 2.0 | - |
| External Managers Fund | 21.9 | 15.8 |
| Floating Rate Note Pool | 7.5 | 11.0 |
| Global Structured Equity Pooled Fund | 21.7 | 16.6 |
| Private Debt Pool | - | 17.3 |
| Private Equity Pool | 13.6 | 13.4 |
| Private Equity Pool (98) | 100.0 | - |
| Private Mortgage Pool | 27.1 | 17.9 |
| Private Real Estate Pool | 23.4 | 8.4 |
| US Passive Equity Pooled Fund | 26.9 | 13.3 |
| United States Pooled Equity Fund | 18.0 | 13.7 |

(a) The Consolidated Cash Investment Trust Fund is managed with the objective of providing competitive interest income to depositors while maintaining maximum security and liquidity of depositors' capital. The portfolio is comprised of high-quality short-term and mid-term fixed-income securities with a maximum term-to-maturity of five years.

(b) Public fixed-income instruments are managed with the objective of providing competitive returns over a four-year period while maintaining maximum security of the Fund's capital. Return is maximized within the risk constraints on the portfolio by management of portfolio duration and issuer mix. Fixed-income securities held by the Fund have an average effective yield of 5.22% per annum based on market for securities maturing between one and twenty years (1998: 5.24% per annum) and the following term structure based on par: 1 to 5 years - 47%; 5 to 10 years - 26%; 10 to 20 years - 27%. As at March 31, 1999, securities with a fair value of $28,646,000 (1998: $106,213,000) were loaned to certain borrowers. The loans were secured by marketable securities with a fair value of $31,370,000 (1998: $112,373,000). During the term of the loan, the Fund retains the right to receive income on the securities loaned, in addition to the fees earned.

(c) The Canadian Dollar Public Debt Pool is managed with the objective of providing above average returns compared to the total return of the Scotia Capital Markets Universe Bond Index over a four-year period while maintaining adequate security and liquidity of participants' capital. The excess return is expected to be achieved through management of portfolio duration and sector rotation. The portfolio is comprised of high quality Canadian fixed-income instruments and debt related derivatives. During the year, the pool received private fixed income securities from the Private Debt Pool and the Private Mortgage Pool. As at March 31, 1999, securities held by the Pool have an average effective yield of 5.51% per annum based on market (1998: 5.41% per annum) and the following term structure based on par: under 1 year - 10%; 1 to 5 years - 37%; 5 to 10 years - 24%; 10 to 20 years - 21%; over 20 years - 8%.

The following is a summary of the Alberta Heritage Savings Trust Fund's investment in the Canadian Dollar Public Debt Pool as at March 31, 1999:

| | 1999 | | 1998 | |
|---|---|---|---|---|
| | Cost | Fair Value | Cost | Fair Value |
| Deposit in the Consolidated Cash Investment Trust Fund | $ 18,797 | $ 18,797 | $ 10,800 | $ 10,800 |
| Public Fixed-income securities: | | | | |
| Government of Canada, direct and guaranteed | 364,229 | 366,823 | 286,770 | 291,346 |
| Province of Alberta, direct and guaranteed | 30,769 | 31,780 | 22,997 | 24,179 |
| Other provinces, direct and guaranteed | 168,520 | 174,009 | 137,271 | 140,556 |
| Municipal | 13,746 | 13,632 | 6,990 | 7,231 |
| Corporate | 544,561 | 527,995 | 375,401 | 363,626 |
| Private Fixed-income Securities | | | | |
| Corporate | 193,991 | 185,052 | - | - |
| Total deposit and fixed-income securities | 1,334,613 | 1,318,088 | 840,229 | 837,738 |
| Accounts receivable and accrued investment income | 32,496 | 32,496 | 14,470 | 14,470 |
| Accounts payable | (16,420) | (16,420) | (6,586) | (6,586) |
| | 16,076 | 16,076 | 7,884 | 7,884 |
| Total - Alberta Heritage Savings Trust Fund | $1,350,689 | $1,334,164 | $ 848,113 | $ 845,622 |
| Total - Canadian Dollar Public Debt Pool | $7,812,035 | $8,112,618 | $6,635,228 | $7,000,911 |

(d) The Floating Rate Note Pool is managed with the objective of generating floating rate income needed for the swap obligations of the participants with structured investments in foreign equities, domestic equities and domestic bonds. Through the use of interest rate swaps the Pool provides investment opportunities in high quality floating-rate instruments with remaining term-to-maturity of ten years or less.

(e) The Private Mortgage Pool is managed with the objective of providing investment returns higher than attainable from the publicly traded bond market over a five to ten year period. The portfolio is comprised primarily of high quality commercial mortgage loans. Risk is reduced by limiting investments to include NHA insured loans and first mortgage loans that provide diversification by property usage. The Pool does not invest in mortgages on single family houses, hotels, motels, trailer parks or recreational properties. As at March 31, 1999, mortgages held by the Pool have an average effective yield of 7.08% per annum based on market (1998: 7.37% per annum) and the following term structure based on par: under 1 year - 9%; 1 to 5 years - 33%; 5 to 10 years - 42%; over 10 years - 16%.

(f) Competitive returns and capital preservation are expected from investments in Canadian public equities. Risk is reduced by prudent security selection and management of holdings in various industrial sectors. As at March 31, 1999, equity securities with a fair value of $99,820,000 (1998: $58,298,000) were loaned to certain borrowers. The loans were secured by marketable securities with a fair value of $109,310,000 (1998: $61,679,000). During the term of the loan, the Fund retains the right to receive income on the securities loaned, in addition to the fees earned.

The following summary of directly held Canadian public equities are listed by industrial classifications used by the Toronto Stock Exchange:

| | 1999 | | | 1998 | | |
|---|---|---|---|---|---|---|
| | Cost | Fair Value | % | Cost | Fair Value | % |
| | ($ thousands) | | | | | |
| Communications and media | $ 16,269 | $ 73,078 | 11 | $ 8,752 | $ 37,280 | 5 |
| Conglomerates | 14,472 | 44,367 | 7 | 14,472 | 55,348 | 8 |
| Consumer products | 5,176 | 26,722 | 4 | 13,800 | 51,357 | 7 |
| Financial services | 4,657 | 20,571 | 3 | 4,657 | 21,655 | 3 |
| Gold and precious minerals | 21,334 | 28,987 | 4 | 21,334 | 37,338 | 5 |
| Industrial products | 49,351 | 135,254 | 21 | 52,797 | 155,264 | 22 |
| Merchandising | 11,543 | 39,900 | 6 | 12,262 | 41,164 | 6 |
| Metals and minerals | 31,479 | 43,202 | 7 | 33,217 | 57,068 | 8 |
| Oil and gas | 36,909 | 62,720 | 10 | 35,844 | 73,893 | 10 |
| Paper and forest products | 12,005 | 15,707 | 2 | 13,471 | 22,897 | 3 |
| Pipelines | 22,748 | 42,891 | 7 | 13,766 | 35,409 | 5 |
| Real estate and construction | 2,667 | 7,873 | 1 | 2,667 | 9,487 | 1 |
| Transportation and environmental services | 14,027 | 16,602 | 3 | 14,027 | 30,814 | 4 |
| Utilities | 37,089 | 93,134 | 14 | 36,923 | 96,871 | 13 |
| | $ 279,726 | $ 651,008 | 100 | $ 277,989 | $ 725,845 | 100 |

(g) The Canadian Pooled Equity Fund is managed with the objective of providing competitive returns comparable to the total return of the Toronto Stock Exchange 300 Index while maintaining maximum preservation of participants' capital. The portfolio is comprised of publicly traded equities in Canadian corporations. Risk is reduced by prudent security selection and sector rotation.

(h) The External Managers Fund is managed by external managers with expertise in global equity markets and Canadian small capitalized companies and large capitalized companies. The objective of the Fund is to provide investment returns higher than the total return of the applicable Morgan Stanley, Standard and Poor's and Toronto Stock Exchange indices over a four-year period. The portfolio is comprised of publicly traded equity securities on Canadian and approved foreign markets. Risk is reduced through manager style and market diversification. The following is a summary of the Alberta Heritage Savings Trust Fund's investment in the External Managers Fund, by geographic region, as at March 31, 1999:

| | 1999 | | 1998 | |
|---|---|---|---|---|
| | Cost | Fair Value | Cost | Fair Value |
| | ($ thousands) | | | |
| Foreign Public Equity Pools: | | | | |
| Multi Region | $ 206,656 | $ 218,518 | $ 140,157 | $ 154,058 |
| Europe | 204,448 | 201,303 | 105,040 | 122,046 |
| Pacific Basin | 104,299 | 132,253 | 75,171 | 68,858 |
| Emerging Markets | 10,158 | 12,083 | - | - |
| | 525,561 | 564,157 | 320,368 | 344,962 |
| United States | 143,616 | 171,535 | 72,737 | 84,832 |
| Canadian | | | | |
| Large capitalized companies | 114,621 | 116,432 | - | - |
| Small capitalized companies | 96,060 | 98,712 | 46,846 | 52,664 |
| | 210,681 | 215,144 | 46,846 | 52,664 |
| Total - Alberta Heritage Savings Trust Fund | $ 879,858 | $ 950,836 | $ 439,951 | $ 482,458 |
| Total - External Managers Fund | $ 3,537,968 | $ 4,338,781 | $ 2,399,553 | $ 3,043,960 |

The following is a summary of assets and liabilities of the External Managers Fund as at March 31, 1999

| | 1999 | 1998 |
|---|---|---|
| | ($ thousands) | |
| Cash and short-term securities | $ 109,079 | $ 130,426 |
| Investments - Public equities | 3,438,393 | 2,270,812 |
| - Fixed-income securities | 1,247 | 3,936 |
| Accounts receivable and accrued investment income | 27,890 | 27,357 |
| Accounts payable | (38,641) | (32,978) |
| Total - External Managers Fund | $ 3,537,968 | $ 2,399,553 |

(i) The Private Equity Pool and the Private Equity Pool (98) are managed with the objective of providing investment returns higher than attainable from the TSE 300 Index over a five to ten year period. The portfolio is comprised of equity investments in companies that show higher than average growth potential. Risk is reduced by avoiding direct investments in start-up and venture capital situations and by limiting holdings in any single company.

(j) The Global Structured Equity Pooled Fund is managed with the objective of providing investment returns comparable to the total return of the Morgan Stanley World Equity Index. The Pool provides exposure to global markets through the use of structured investments such as foreign equity index swaps and as at March 31, 1999, 90% (1998: 81%) of the Pool's underlying investments supporting the index swaps are held in units of the Floating Rate Note Pool [see Schedule 1 (d)].

(k) The US Passive Equity Pooled Fund is a passively managed United States equity fund that provides a return equal to the total rate of the Standard & Poor's 500 United States Equity Index. Futures, swaps and other structured investments may be used to enhance performance of the fund.

(l) The Private Real Estate Pool is managed with the objective of providing investment returns comparable to the Russell Canadian Property Index over a five to ten year period. Real estate is held through intermediate companies which have issued to the Pool, common shares and participating debentures secured by a charge on real estate. Risk is reduced by investing in properties that provide diversification by geographic location, by property type and by tenancy. As real estate returns are positively correlated to inflation and negatively correlated to returns from fixed income securities and equities, the Pool provides diversification from the securities market with opportunities for high return.

(m) Deposits and Floating Rate Note Pool units are used as the underlying securities to support the index swaps issued by the Fund (see Note 4). If the effect of the swaps were reflected in this schedule, deposit and fixed-income securities would be reduced by $142,069,000 (1998: $159,924,000) and Canadian equities increased by a corresponding amount. The resulting assets mix percentage would be 43.5% fixed income and 56.5% equities.

(n) See Schedule 2, note (f).

Schedule 2

# ALBERTA HERITAGE SAVINGS TRUST FUND
## SCHEDULE OF TRANSITION PORTFOLIO INVESTMENTS
## MARCH 31, 1999
($ thousands)

| | 1999 | | | 1998 | | |
|---|---|---|---|---|---|---|
| | Cost | Fair Value | % | Cost | Fair Value | % |
| Deposit in the Consolidated Cash Investment | | | | | | |
| Trust Fund (a) | $ 45,010 | $ 45,010 | 0.6 | $ 78,612 | $ 78,612 | 0.7 |
| Fixed-income securities: | | | | | | |
| Public, directly held (b) | | | | | | |
| Government of Canada, direct and guaranteed | 2,189,957 | 2,222,780 | 27.4 | 2,401,344 | 2,463,997 | 26.7 |
| Provincial: | | | | | | |
| Alberta, direct and guaranteed | 132,129 | 134,188 | 1.7 | 208,133 | 212,104 | 2.3 |
| Other, direct and guaranteed | 1,810,526 | 1,851,512 | 22.8 | 1,991,993 | 2,085,971 | 22.6 |
| Municipal | 71,888 | 75,165 | 0.9 | 61,704 | 64,671 | 0.7 |
| Corporate | 2,858,237 | 2,894,530 | 35.6 | 2,908,280 | 2,947,935 | 32.0 |
| Total deposit and fixed-income securities, public | 7,107,747 | 7,223,185 | 89.0 | 7,650,066 | 7,853,290 | 85.0 |
| Provincial corporation debentures (c): | | | | | | |
| Agriculture Financial Services Corporation | 401,212 | 426,483 | 5.2 | 576,900 | 617,717 | 6.7 |
| Alberta Social Housing Corporation | 230,558 | 326,252 | 4.0 | 476,444 | 587,703 | 6.5 |
| Alberta Municipal Financing Corporation | 140,000 | 149,317 | 1.8 | 140,000 | 158,631 | 1.7 |
| Alberta Opportunity Company | - | - | - | 5,977 | 6,081 | 0.1 |
| Total Provincial corporation debentures | 771,770 | 902,052 | 11.0 | 1,199,321 | 1,370,132 | 15.0 |
| Total deposit, debentures and fixed-income securities | 7,879,517 | $8,125,237 | 100.0 | 8,849,387 | $9,223,422 | 100.0 |
| Canadian equities: | | | | | | |
| Public, directly held: | | | | | | |
| TransCanada Pipelines Limited | 53,966 | $ 63,812 | | - | $ - | |
| NOVA Chemical Ltd. | 11,714 | 16,077 | | - | - | |
| NOVA Corporation of Alberta Ltd. | - | - | | 112,283 | 181,276 | |
| Total Canadian equities | 65,680 | $ 79,889 | | 112,283 | $ 181,276 | |
| Loans: | | | | | | |
| Ridley Grain Ltd. | | | | | | |
| [11.303% due July 31, 2015 (d)] | 93,500 | | | 97,750 | | |
| Vencap Acquisition Corporation (e) | | | | | | |
| due 2001and 2046 | 14,317 | | | 12,498 | | |
| Murphy Oil Company Ltd. | - | | | 37,970 | | |
| Alberta Pacific Pulp Mill Project | - | | | 260,000 | | |
| Total loans | 107,817 | | | 408,218 | | |
| Total investments (f) | $8,053,014 | | | $9,369,888 | | |

(a) See Schedule 1, note (a).

(b) Public fixed-income instruments are managed with the objective of providing a market rate of return higher than the market cost of the Canadian dollar portion of the Province's debt portfolio on an annual basis. Any excess return is expected to be achieved through management of portfolio duration as well as through issuer mix. As at March 31, 1999, fixed-income securities held have an average effective yield of 4.91% per annum based on market value for securities maturing within a year (1998: 4.84% per annum), and 5.30% per annum for securities maturing between 1 and 35 years (1998: 5.34% per annum). As at March 31, 1999, the securities have the following term structure based on par: under 1 year - 10%; 1 to 5 years - 56%; 5 to 10 years - 33%; over 10 years - 1%. As at March 31, 1999, securities with a fair value of $857,691,000 (1998: $660,737,000) were loaned to certain borrowers. The loans were secured by marketable securities with a fair value of $939,235,000 (1998:$699,059,000). During the term of the loan, the Fund retains the right to receive income on the securities loaned, in addition to the fees earned.

(c) As at March 31, 1999, Provincial corporation debentures have an average effective yield of 7.52% per annum based on market value (1998: 7.41% per annum). The maturity profile based on expected repayments is as follows: under 1 year \$259,216,000; 1 to 5 years \$417,897,000; and over 5 years \$94,657,000. Interest rates on Alberta Municipal Financing Corporation debentures are fixed to maturity and redemption is by a single payment of the full principal sum on maturity. In general the interest rates on the other provincial corporation debentures are fixed for a five year period only and repayment is by either semi-annual or annual instalments of the principal sum over the life of the debenture. The Province, through the General Revenue Fund, plans to borrow funds in the market and lend the funds to Agriculture Financial Services Corporation (AFSC) and lend or grant funds to Alberta Social Housing Corporation (ASHC). AFSC and ASHC will use the funds to repay the debentures held by the Transition Portfolio generally on the dates when the interest rates on these debentures are reset (every five years). During the year, debentures amounting to \$350,725,000 (1998: \$496,815,000) were redeemed prior to maturity.

The Fund's investment in provincial corporation debentures is summarized below:

| | 1999 | 1998 |
|---|---|---|
| | ($ thousands) | |
| Balance at beginning of year | $ 1,199,321 | $ 1,798,037 |
| Disposals, repayments and redemptions: | | |
| Agriculture Financial Services Corporation | (175,688) | (158,751) |
| Alberta Social Housing Corporation | (245,886) | (427,201) |
| Alberta Opportunity Company | (5,977) | (12,764) |
| Balance at end of year | $ 771,770 | $ 1,199,321 |

Fair values of Provincial corporation debentures are based on the net present value of future cash flows. Each individual cash flow payment is discounted at a rate which matches the term of the cash flow payment and is adjusted for a yield premium to reflect several factors. These include a liquidity premium to reflect the fact that if the debentures are sold, there will be a limited pool of these securities trading in the market; that the debentures would be new to the market and are not direct issues of the Province; a premium for the periodic interest reset feature where applicable; and a factor to reflect the blended payment structure of the debenture.

(d) Under the terms of the loans, prior to July 31, 1985, interest on the loans has been capitalized and compounded annually; thereafter interest is compounded semi-annually and payable annually to the extent of available cash flow for that purpose, and any shortfall is to be capitalized. The principal, including capitalized interest, is repayable on or before July 31, 2015. As at March 31, 1999 the allowance for credit losses amounted to \$42,927,000 (1998: \$42,927,000).

Grain throughput volumes are the main determinant of profitability of the grain terminal and its ability to service its loan from the province, and therefore the value is sensitive to changes in grain throughput volumes. Grain throughputs are difficult to forecast because they are dependent in part upon port allocation decisions of the Canadian Wheat Board and a number of other factors such as crop size and composition.

(e) In October 1995, the Province agreed to terms of an Arrangement Agreement with Vencap Equities Alberta Ltd. (Vencap) and Vencap Acquisition Corporation, an indirect wholly owned subsidiary of Onex Corporation. Pursuant to this Agreement, the province sold its \$199,989,000 Vencap loan and 4 million Vencap share options for cash of \$166 million and non-interest bearing payments totaling \$63,988,000 rescheduled on amended terms as follows:

- \$11,400,000 is repayable in January 2001, and will bear no interest.
- The balance of \$52,588,000 is repayable in July 2046, and will also bear no interest.

The carrying value of the loan has been adjusted to an amount equal to the present value of anticipated loan repayments.

The discount is amortized to investment income over the remaining term of the loan on a straight-line basis.

(f) During the period, investments with a cost of \$1,205,447,000 (market \$1,207,196,000), including \$1,200,000,000 in deposits in the Consolidated Cash Investment Trust Fund and \$5,447,000 in equities, were transferred from the Transition Portfolio to the Endowment Portfolio in accordance with the investment provisions of the Alberta Heritage Savings Trust Fund Act.

## ALBERTA HERITAGE SCHOLARSHIP FUND
## FINANCIAL STATEMENTS
## MARCH 31, 1999



## AUDITOR'S REPORT

To the Provincial Treasurer

I have audited the balance sheet of the Alberta Heritage Scholarship Fund as at March 31, 1999 and the statements of income and retained earnings and changes in financial position for the year then ended. These financial statements are the responsibility of the Fund's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In my opinion, these financial statements present fairly, in all material respects, the financial position of the Fund as at March 31, 1999 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles.

Peter Valentine, FCA
Auditor General

Edmonton, Alberta
May 21, 1999

## ALBERTA HERITAGE SCHOLARSHIP FUND
## BALANCE SHEET
## MARCH 31, 1999
($ thousands)

| | 1999 | 1998 |
|---|---|---|
| **ASSETS** | | |
| Portfolio investments (Note 3) | $ 275,876 | $ 248,114 |
| Accrued interest and accounts receivable | - | 1,162 |
| | $ 275,876 | $ 249,276 |
| **LIABILITIES, ENDOWMENT AND RETAINED EARNINGS** | | |
| Liabilities: | | |
| Payable to the Province of Alberta | $ 7 | $ 27 |
| Accounts payable | - | 106 |
| | 7 | 133 |
| Endowment (Note 6) | 100,000 | 100,000 |
| Retained earnings (Note 6) | 175,869 | 149,143 |
| | $ 275,876 | $ 249,276 |

The accompanying notes and schedules are part of these financial statements.

## ALBERTA HERITAGE SCHOLARSHIP FUND
## STATEMENT OF INCOME AND RETAINED EARNINGS
## FOR THE YEAR ENDED MARCH 31, 1999
($ thousands)

| | 1999 | | 1998 |
|---|---|---|---|
| | Budget | Actual | Actual |
| Income: | | | |
| Investment income (Note 7) | $ 20,000 | $ 38,951 | $ 37,086 |
| Contributions from Province of Alberta | 200 | 200 | 200 |
| Other contributions | 120 | 180 | 38 |
| | 20,320 | 39,331 | 37,324 |
| Expenses: | | | |
| Scholarships | 13,000 | 12,480 | 11,938 |
| Administrative expenses (Note 8) | 120 | 125 | 98 |
| | 13,120 | 12,605 | 12,036 |
| Net income | $ 7,200 | 26,726 | 25,288 |
| Retained earnings at beginning of year | | 149,143 | 123,855 |
| Retained earnings at end of year | | $ 175,869 | $ 149,143 |

# ALBERTA HERITAGE SCHOLARSHIP FUND
## STATEMENT OF CHANGES IN FINANCIAL POSITION
## FOR THE YEAR ENDED MARCH 31, 1999
($ thousands)

| | 1999 | 1998 |
|---|---|---|
| Operating transactions: | | |
| Net income | $ 26,726 | $ 25,288 |
| Non-cash items included in net income | (18,493) | (9,991) |
| | 8,233 | 15,297 |
| Decrease in receivables | 1,162 | 17 |
| Decrease in payables | (126) | (13) |
| Cash provided by operating transactions | 9,269 | 15,301 |
| Investing transactions | | |
| Proceeds from disposals, repayments and redemptions of investments | 143,462 | 51,879 |
| Purchase of investments | (156,048) | (75,337) |
| Cash applied to investing transactions | (12,586) | (23,458) |
| Decrease in cash and cash equivalents | (3,317) | (8,157) |
| Cash and cash equivalents at beginning of year | 8,537 | 16,694 |
| Cash and cash equivalents at end of year | $ 5,220 | $ 8,537 |
| Consisting of Deposit in the Consolidated Cash Investment Trust Fund (Note 3) | $ 5,220 | $ 8,537 |

# ALBERTA HERITAGE SCHOLARSHIP FUND
## NOTES TO THE FINANCIAL STATEMENTS
## MARCH 31, 1999

Note 1 Authority and Purpose

The Alberta Heritage Scholarship Fund ("the Fund") operates under the authority of the Alberta Heritage Scholarship Act, Chapter A-27.1, Statutes of Alberta 1981.

The purpose of the Fund is to pool and invest the endowment and other contributions made to the Fund. The Fund has been managed with the objectives of providing an annual level of income for scholarships while preserving the capital of the endowment over the long term. The portfolio is comprised of high quality fixed-income securities and equities.

Note 2 Significant Accounting Policies and Reporting Practices

These financial statements are prepared in accordance with generally accepted accounting principles.

The accounting policies of significance to the Fund are as follows:

(a) Portfolio Investments

Fixed-income securities, mortgages and equities held either directly by the Fund or by pooled investment funds are recorded at cost. Cost includes the amount of applicable amortization of discount or premium using the straight-line method over the life of the investments.

The cost of disposals is determined on the average cost basis.

Where there has been a loss in value of an investment that is other than a temporary decline, the investment is written down to recognize the loss. The written down value is deemed to be the new cost.

(b) Income

Investment income is recorded on the accrual basis. Income and expense on index swaps and interest rate swaps are accrued as earned and gains and losses arising as a result of disposals are included in the determination of investment income.

(c) Foreign Currency

Foreign currency transactions are translated into Canadian dollars using average rates of exchange, except for hedged foreign currency transactions which are translated at rates of exchange established by the terms of the forward exchange contracts. Exchange differences on unhedged transactions are included in the determination of investment income.

(d) Investment Valuation

Fair value is the amount of consideration agreed upon in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act. Fair values of investments held either by the Fund or by pooled investment funds are determined as follows:

(i) Public fixed-income securities and equities are valued at the year-end closing sale price, or the average of the latest bid and ask prices quoted by an independent securities valuation company.

(ii) Private fixed-income securities and mortgages are valued based on the net present value of future cash flows. These cash flows are discounted using Government of Canada bond rates adjusted for a risk premium estimated by management.

(iii) The fair value of private equities is estimated by management.

(iv) The fair values of deposits, receivables, accrued interest and payables are estimated to approximate their book values.

(v) The fair value of investments and any other assets and liabilities denominated in a foreign currency are translated at the year-end exchange rate.

Note 3 Portfolio Investments

Portfolio investments are summarized as follows:

| | 1999 | | | 1998 | | |
|---|---|---|---|---|---|---|
| | Cost | Fair Value | % | Cost | Fair Value | % |
| | | | ($ thousands) | | | |
| Deposit in the Consolidated Cash Investment Trust Fund (a) | $ 5,220 | $ 5,220 | 1.7 | $ 8,537 | $ 8,537 | 2.8 |
| Fixed-income securities: | | | | | | |
| Public, directly held (b) | | | | | | |
| Government of Canada, direct and guaranteed | 1,223 | 1,223 | 0.4 | 59,164 | 71,063 | 23.2 |
| Province of Alberta, guaranteed | - | - | - | 1,054 | 1,171 | 0.4 |
| Other provinces direct and guaranteed | - | - | - | 5,660 | 6,198 | 2.0 |
| Municipal | - | - | - | 456 | 508 | 0.2 |
| Corporate | - | - | - | 150 | 168 | 0.1 |
| Canadian Dollar Public Debt Pool (Schedule 1) | 104,349 | 103,554 | 33.9 | 31,014 | 31,327 | 10.2 |
| Private Mortgage Pool (c) | 7,257 | 8,488 | 2.8 | 5,308 | 7,033 | 2.3 |
| Private Debt Pool | - | - | - | 12,498 | 12,952 | 4.2 |
| Total deposit and fixed-income securities | 118,049 | 118,485 | 38.8 | 123,841 | 138,957 | 45.4 |
| Canadian equities: | | | | | | |
| Canadian Pooled Equity Fund (Schedule 2) | 22,801 | 33,598 | 11.0 | 23,587 | 39,971 | 13.1 |
| Domestic Passive Equity Pooled Fund (Schedule 3) | 26,100 | 32,949 | 10.8 | 6,018 | 5,963 | 2.0 |
| External Managers Fund (Canadian)(Schedule 4) | 17,339 | 17,534 | 5.7 | 9,461 | 11,864 | 3.9 |
| Private Equity Pool (d) | 927 | 1,792 | 0.6 | 1,559 | 2,962 | 1.0 |
| Transition Account | | | | 22,448 | 36,433 | 11.9 |
| Foreign equities: | | | | | | |
| External Managers Fund (Global) (Schedule 4) | 33,428 | 38,753 | 12.7 | 29,817 | 33,989 | 11.1 |
| Global Structured Equity Pooled Fund (e) | 35,188 | 35,435 | 11.6 | 19,043 | 19,557 | 6.4 |
| US Passive Equity Pooled Fund (f) | 9,493 | 9,939 | 3.3 | 7,586 | 7,868 | 2.6 |
| External Managers Fund (United States) (Schedule 4) | 5,640 | 10,041 | 3.3 | 4,439 | 7,458 | 2.4 |
| United States Pooled Equity Fund | 178 | 142 | - | 315 | 633 | 0.2 |
| Real Estate: | | | | | | |
| Private Real Estate Pool (g) | 6,733 | 6,737 | 2.2 | - | - | - |
| | 157,827 | 186,920 | 61.2 | 124,273 | 166,698 | 54.6 |
| Total investments | $275,876 | $305,405 | 100.0 | $248,114 | $305,655 | 100.0 |

The majority of the Fund's investments are held in pooled investment funds established and administered by the Provincial Treasurer. Pooled investment funds have a market based unit value that is used to allocate income to participants and to value purchases and sales of pool units. As at March 31, 1999, the Fund's percentage ownership, at market, in pooled investment funds is as follows:

| | % Ownership | |
|---|---|---|
| | 1999 | 1998 |
| Canadian Dollar Public Debt Pool | 1.3 | 0.4 |
| Canadian Pooled Equity Fund | 1.6 | 1.7 |
| Domestic Passive Equity Pooled Fund | 1.6 | 1.1 |
| External Managers Fund | 1.5 | 1.7 |
| Global Structured Equity Pooled Fund | 2.6 | 1.9 |
| Private Debt Pool | - | 1.7 |
| Private Equity Pool | 2.2 | 2.2 |
| Private Mortgage Pool | 0.8 | 0.9 |
| Private Real Estate Pool | 0.9 | - |
| Transition Account | - | 2.2 |
| US Passive Equity Pooled Fund | 1.6 | 1.7 |
| United States Pooled Equity Fund | 1.6 | 1.7 |

(a) The Consolidated Cash Investment Trust Fund is managed with the objective of providing competitive interest income to depositors while maintaining maximum security and liquidity of depositors' capital. The portfolio is comprised of high-quality short-term and mid-term fixed-income securities with a maximum term to maturity of five years.

(b) As at March 31, 1999, short-term public fixed income securities have an average effective yield of 4.75% per annum based on market (1998: 4.73% per annum). At March 31, 1999, securities with a fair value of $1,073,000 (1998: $9,266,000) were loaned to certain borrowers. The loans were secured by marketable securities with a fair value of $1,175,000 (1998: $9,803,000). During the term of the loans, the Fund retains the right to receive income on the investments loaned, in addition to the fee earned.

(c) The Private Mortgage Pool is managed with the objective of providing investment returns higher than attainable from the publicly traded bond market over a five to ten year period. The portfolio is comprised primarily of high quality commercial mortgage loans. Risk is reduced by limiting investments to include only NHA insured loans and first mortgage loans that provide diversification by property usage. The Pool does not invest in mortgages on single family houses, hotels, motels, trailer parks or recreational properties. As at March 31, 1999, mortgages held by the Pool have an average effective yield of 7.08% per annum based on market (1998: 7.37% per annum) and the following term structure based on par: under 1 year - 9%; 1 to 5 years - 33%; 5 to 10 years - 42%; over 10 years - 16%.

(d) The Private Equity Pool is managed with the objective of providing investment returns higher than attainable from the TSE 300 Index over a five to ten year period. The portfolio is comprised of equity investments in companies that show higher than average growth potential. Risk is reduced by avoiding direct investments in start-up and venture capital situations and by limiting holdings in any single company.

(e) The Global Structured Equity Pooled Fund is managed with the objective of providing investment returns comparable to the total return of the Morgan Stanley World Equity Index. The Pool provides exposure to global markets through the use of structured investments such as foreign equity index swaps and as at March 31, 1999, 90% (1998: 81%) of the Pool's underlying investments supporting the index swaps are held in units of the Floating Rate Note Pool [see Schedule 3 (a)].

(f) The US Passive Equity Pooled Fund is a passively managed United States equity fund that provides a return equal to the total return of the Standard & Poor's 500 United States Equity Index. Futures, swaps and other structured investments may be used to enhance performance of the fund.

(g) The Private Real Estate Pool is managed with the objective of providing investment returns comparable to the Russell Canadian Property Index over a five to ten year period. Real Estate is held through intermediate companies which have issued to the pool, common shares and participating debentures secured by a charge on real estate. Risk is reduced by investing in properties that provide diversification by geographic location, by property type and by tenancy. As real estate returns are positively correlated to inflation and negatively correlated to returns from fixed income securities and equities, the pool provides diversification from the securities market with opportunities for high returns.

Note 4 Investment Risk Management

Income and financial returns of the Fund are exposed to credit risk and price risk. Credit risk relates to the possibility that a loss may occur from the failure of another party to perform according to the terms of a contract. Price risk is comprised of currency risk, interest rate risk and market risk. Currency risk relates to the possibility that the investments will change in value due to future fluctuations in foreign exchange rates. Interest rate risk relates to the possibility that the investments will change in value due to future fluctuations in market interest rates. Market risk relates to the possibility that the investments will change in value due to future fluctuations in market prices.

In order to earn an optimal financial return at an acceptable level of risk, management of the Fund has established a policy asset mix of 35% to 65% fixed-income instruments and 35% to 65% equities. Risk is reduced through asset class diversification, diversification within each asset class, quality constraints on fixed-income instruments, and restrictions on amounts exposed to countries designated as emerging markets. Borrowing or leveraging is not allowed with the exception of pre-existing mortgages on real estate properties. Controls are in place respecting the use of derivatives (see Note 5). Forward foreign exchange contracts may be used to manage currency exposure in connection with securities purchased in foreign currency (see Note 5).

Note 5 Index Swaps, Interest Rate Swaps, Foreign Exchange and Futures Contracts

The Fund uses index and interest rate swaps directly, or indirectly through pooled funds to enhance return. A swap is a contractual agreement between two parties to exchange a series of cash flows based on a notional amount and does not involve the exchange of the underlying principal.

An index swap involves the exchange of a floating interest rate cash flow for one based on the performance of a market index. For interest rate swaps, parties generally exchange fixed and floating rate interest cash flows based on a notional value. Notional value is the amount to which a rate or price is applied in order to calculate the exchange of cash flows. All swaps are supported by underlying securities. Leveraging is not allowed.

The following is a summary of the Fund's proportionate share of the notional value of index and interest rate swaps held directly or issued by pooled funds as at March 31, 1999.

| | 1999 | 1998 |
|---|---|---|
| | ($ thousands) | |
| Index swaps: | | |
| Foreign equities (Global Structured Equity Pooled Fund) | $ 34,825 | $ 19,197 |
| Bonds (Canadian Dollar Public Debt Pool) | 19,429 | 5,697 |
| Canadian equities (Domestic Passive Equity Pooled Fund) | 12,596 | 3,484 |
| United States equities (US Passive Equity Pooled Fund) | 9,813 | 7,425 |
| Canadian equities (Transition Account) | - | 4,636 |
| Interest rate swaps: | | |
| Global Structured Equity Pooled Fund | 24,800 | 11,012 |
| Canadian Dollar Public Debt Pool | 13,963 | 2,852 |
| Domestic Passive Equity Pooled Fund | 9,571 | 1,457 |
| US Passive Equity Pooled Fund | 889 | |
| Transition Account | - | 1,528 |
| Total | $ 125,886 | $ 57,288 |

Fair values of swaps have been included in the determination of the fair values of the respective pooled investment funds. Credit exposure relating to swaps is minimal as management deals only with the most credit worthy counterparties.

Foreign exchange contracts are contractual agreements to exchange specified currencies at an agreed upon exchange rate and on an agreed settlement date in the future. As at March 31, 1999, the Fund's proportionate share of outstanding forward foreign exchange contracts issued by the External Managers Fund amounted to $9,592,000 (1998: $6,215,000).

A stock index futures contract is an agreement to take or make delivery of an amount of cash reflecting the difference between changes in the level of the specified stock index. As at March 31, 1999, the notional value of stock index futures contracts issued by the External Managers Fund amounted to $396,000 (1998: $Nil).

Note 6 Endowment and Retained Earnings

The endowment was received from the Alberta Heritage Savings Trust Fund on June 18, 1981. The Alberta Heritage Scholarship Act provides that money required by the Students Finance Board for providing scholarships or for paying the costs of administering scholarships, shall be paid from the Fund, but no portion of the original endowment may be paid out of the Fund.

As at March 31, 1999, the fair value of endowment and retained earnings amounted to approximately $305,398,000 (1998: $306,684,000).

Note 7 Investment Income

| | 1999 | 1998 |
|---|---|---|
| | ($ thousands) | |
| Deposit and fixed-income securities: | | |
| Deposit in the Consolidated Cash Investment Trust Fund | $ 367 | $ 300 |
| Public fixed-income securities, directly held | | |
| Government of Canada, direct and guaranteed | 12,989 | 5,232 |
| Alberta, direct and guaranteed | 127 | 104 |
| Other provincial, direct and guaranteed | 656 | 581 |
| Municipal | 56 | 73 |
| Corporate | 6 | 15 |
| Security lending | 2 | 11 |
| Canadian Dollar Public Debt Pool | 6,889 | 3,168 |
| Private Debt Pool | 832 | 306 |
| Private Mortgage Pool | 1,187 | 583 |
| | 23,111 | 10,373 |
| Equities: | | |
| Canadian Pooled Equity Fund | 3,084 | 8,809 |
| Transition Account | 558 | 1,430 |
| Domestic Passive Equity Pooled Fund | 1,148 | 1,018 |
| External Managers Fund (Canadian) | (14) | 498 |
| Private Equity Pool | 246 | 464 |
| External Managers Fund (Global) | 3,494 | 2,470 |
| Global Structured Equity Pooled Fund | 4,144 | 4,766 |
| United States Pooled Equity Fund | 149 | 6,090 |
| US Passive Equity Pooled Fund | 1,879 | 88 |
| External Managers Fund (United States) | 1,061 | 1,080 |
| Private Real Estate Pool | 91 | - |
| | 15,840 | 26,713 |
| Investment income | $ 38,951 | $ 37,086 |

Investment income is comprised of interest, dividends, amortization of discount or premium, swap income, security lending income and realized gains and losses, net of write-downs on investments. The Fund's share of income earned from pooled investment funds is net of administrative expenses incurred by the pool (see Note 8).

Investment income includes net gains from disposal of investments totalling $24,066,000 (1998: $20,933,000).

Note 8 Administrative Expenses

Administrative expenses include investment management, cash management and safekeeping costs charged on a cost-recovery basis directly by the Department of Treasury. External management and custodial fees are deducted directly from investment income of the External Managers Fund (Canadian, Global and United States). During the year, the Fund's share of administrative expenses deducted directly from investment income of externally and internally managed pooled funds (see Note 7) amounted to $245,000 and $34,000 respectively (1998: $213,000 and $20,000). Total administrative expense during the year, including amounts deducted directly from investment income of pooled funds, amounted to $404,000 (1998: $331,000).

Note 9 Uncertainty Due to the Year 2000

The year 2000 issue is the result of some computer systems using two digits rather than four to define the applicable year. Government computer systems that have date sensitive software may recognize a date using "00" as the year 1900 rather than the year 2000, which could result in miscalculations or system failures. In addition, similar problems may arise in some systems if certain dates in 1999 are not recognized as a valid date or are recognized to represent something other than a date. The effects of the year 2000 issue may be experienced before, on, or after January 1, 2000. If not addressed, the effect on operations and financial reporting may range from minor errors to significant systems failure that could affect the ability to conduct some government operations. Despite the government's efforts to address this issue, it is not possible to be certain that all aspects of the year 2000 issue affecting the Fund, including those related to the efforts of customers, suppliers and other third parties, will be fully resolved.

Note 10 Comparative Figures

Certain 1998 figures have been reclassified to conform to 1999 presentation.

Note 11 Approval of Financial Statements

These financial statements were approved by management.

Schedule 1

# ALBERTA HERITAGE SCHOLARSHIP FUND
## SCHEDULE OF INVESTMENTS IN CANADIAN DOLLAR PUBLIC DEBT POOL
### MARCH 31, 1999

($ thousands)

| | 1999 | | 1998 | |
|---|---|---|---|---|
| | Cost | Fair Value | Cost | Fair Value |
| Deposit in the Consolidated Cash Investment Trust Fund | $ 1,459 | $ 1,459 | $ 400 | $ 400 |
| Public fixed-income securities (b) | | | | |
| Government of Canada, direct and guaranteed | 28,135 | 28,472 | 10,483 | 10,793 |
| Provincial: | | | | |
| Alberta, direct and guaranteed | 2,377 | 2,467 | 841 | 896 |
| Other, direct and guaranteed | 13,018 | 13,505 | 5,018 | 5,207 |
| Municipal | 1,062 | 1,058 | 256 | 268 |
| Corporate | 42,066 | 40,982 | 13,724 | 13,471 |
| Private fixed-income securities | | | | |
| Corporate | 14,984 | 14,363 | - | - |
| | 103,101 | 102,306 | 30,722 | 31,035 |
| Accrued interest and accounts receivable | 2,522 | 2,522 | 536 | 536 |
| Accounts payable | (1,274) | (1,274) | (244) | (244) |
| | 1,248 | 1,248 | 292 | 292 |
| Total - Alberta Heritage Scholarship Fund | $ 104,349 | $ 103,554 | $ 31,014 | $ 31,327 |
| Total - Canadian Dollar Public Debt Pool (a) | $ 7,812,035 | $ 8,112,618 | $ 6,635,228 | $ 7,000,911 |

(a) The Canadian Dollar Public Debt Pool is managed with the objective of providing competitive returns comparable to the total return of the Scotia Capital Markets Universe Bond Index over a four-year period while maintaining adequate security and liquidity of participants' capital. The portfolio is comprised of high quality Canadian fixed income instruments and debt related derivatives. Competitive returns are achieved through management of the portfolio duration and sector rotation.

(b) As at March 31, 1999, securities held by the pool have an average effective yield of 5.51% per annum based on market (1998: 5.41% per annum) and the following term structure based on par: under 1 year - 10%; 1 to 5 years - 37%; 5 to 10 years - 24%; 10 to 20 years - 21%; over 20 years - 8%.

# ALBERTA HERITAGE SCHOLARSHIP FUND
## SCHEDULE OF INVESTMENTS IN CANADIAN POOLED EQUITY FUND
## MARCH 31, 1999

($ thousands)

| | 1999 | | 1998 | |
|---|---|---|---|---|
| | Cost | Fair Value | Cost | Fair Value |
| Deposit in the Consolidated Cash Investment Trust Fund | $ 199 | $ 199 | $ 1,334 | $ 1,334 |
| Canadian public equities (b): | | | | |
| Common shares and rights: | | | | |
| Communications and media | 1,196 | 2,289 | 428 | 978 |
| Conglomerates | 1,147 | 1,881 | 1,221 | 2,411 |
| Consumer products | 1,119 | 1,617 | 787 | 1,315 |
| Financial services | 4,412 | 7,158 | 3,759 | 8,177 |
| Gold and precious minerals | 1,407 | 1,467 | 1,301 | 1,755 |
| Industrial products | 4,217 | 6,893 | 2,924 | 5,934 |
| Merchandising | 574 | 828 | 617 | 1,098 |
| Metals and minerals | 1,143 | 1,097 | 1,637 | 1,912 |
| Oil and gas | 2,308 | 2,521 | 4,748 | 5,925 |
| Paper and forest products | 601 | 673 | 784 | 1,114 |
| Pipelines | 648 | 877 | 531 | 1,000 |
| Real estate and construction | 718 | 809 | 510 | 710 |
| Transportation and environmental services | 739 | 847 | 920 | 1,819 |
| Utilities | 2,099 | 4,072 | 1,734 | 4,040 |
| Passive index | 346 | 442 | 255 | 352 |
| | 22,674 | 33,471 | 22,156 | 38,540 |
| Accrued interest and accounts receivable | 209 | 209 | 97 | 97 |
| Accounts payable | (281) | (281) | - | - |
| | (72) | (72) | 97 | 97 |
| Total - Alberta Heritage Scholarship Fund | $ 22,801 | $ 33,598 | $ 23,587 | $ 39,971 |
| Total - Canadian Pooled Equity Fund (a) | $ 1,788,730 | $ 2,045,408 | $ 1,841,419 | $ 2,327,728 |

(a) The Canadian Pooled Equity Fund is managed with the objective of providing competitive returns comparable to the total return of the Toronto Stock Exchange 300 Index. The portfolio is comprised of publicly traded equities in Canadian corporations. Risk is reduced by prudent security selection and sector rotation.

(b) The industrial classifications are those used by the Toronto Stock Exchange.

# ALBERTA HERITAGE SCHOLARSHIP FUND
## SCHEDULE OF INVESTMENTS IN DOMESTIC PASSIVE EQUITY POOLED FUND
## MARCH 31, 1999

($ thousands)

| | 1999 | | 1998 | |
|---|---|---|---|---|
| | Cost | Fair Value | Cost | Fair Value |
| Deposit in the Consolidated Cash Investment Trust Fund | $ 111 | $ 111 | $ 70 | $ 70 |
| Fixed-income securities, corporate | 168 | 210 | 224 | 201 |
| Floating Rate Note Pool | 8,564 | 10,692 | 1,354 | 1,225 |
| | 8,843 | 11,013 | 1,648 | 1,496 |
| Canadian public equities (b): | | | | |
| Common shares and rights: | | | | |
| Communications and media | 1,003 | 1,679 | 134 | 161 |
| Conglomerates | 495 | 624 | 74 | 93 |
| Consumer products | 666 | 904 | 138 | 142 |
| Financial services | 2,581 | 3,825 | 346 | 523 |
| Gold and precious minerals | 1,137 | 880 | 255 | 154 |
| Industrial products | 2,762 | 3,920 | 382 | 467 |
| Merchandising | 613 | 791 | 104 | 120 |
| Metals and minerals | 852 | 652 | 148 | 106 |
| Oil and gas | 2,047 | 1,866 | 369 | 345 |
| Paper and forest products | 562 | 585 | 107 | 96 |
| Pipelines | 428 | 512 | 37 | 52 |
| Real estate and construction | 414 | 436 | 50 | 55 |
| Transportation and environmental services | 388 | 414 | 58 | 75 |
| Utilities | 1,329 | 2,402 | 186 | 271 |
| Passive index | 265 | 332 | 62 | 63 |
| | 15,542 | 19,822 | 2,450 | 2,723 |
| Domestic Structured Equity Pooled Fund | 1,632 | 2,024 | 1,710 | 1,534 |
| United States Public Equities | 30 | 37 | - | - |
| Accrued interest and accounts receivable | 107 | 107 | 218 | 218 |
| Accounts payable | (54) | (54) | (8) | (8) |
| | 53 | 53 | 210 | 210 |
| Total - Alberta Heritage Scholarship Fund | $ 26,100 | $ 32,949 | $ 6,018 | $ 5,963 |
| Total - Domestic Passive Equity Pooled Fund (a) | $ 1,983,918 | $ 2,005,862 | $ 493,372 | $ 539,403 |

(a) The Domestic Passive Equity Pooled Fund is managed on a passive approach with the objective of providing investment returns comparable to the Toronto Stock Exchange (TSE) 300 Index. The portfolio is comprised of publicly traded equities in Canadian corporations similar in weights to the TSE 300 Index. To enhance investment returns with no substantial increase in risks, the pooled fund invests in the Domestic Structured Equity Pooled Fund (DSEP) and the Floating Rate Note Pool (FRNP) which are pooled investment funds established and administered by the Provincial Treasurer. DSEP provides exposure to the Canadian equity markets through the use of structured investments such as index swaps and interest rate swaps. It provides returns comparable to the TSE indices. FRNP is managed with the objective of generating floating rate income needed for the swap obligations of the participants with structured investments in equities and bonds. Through the use of structured investments such as interest rate swaps, FRNP provides investment opportunities in high quality floating rate instruments with remaining term-to-maturity of ten years or less.

(b) The industrial classifications are those used by the Toronto Stock Exchange.

Schedule 4

# ALBERTA HERITAGE SCHOLARSHIP FUND
## SCHEDULE OF INVESTMENTS IN EXTERNAL MANAGERS FUND
## MARCH 31, 1999

($ thousands)

| | 1999 | | 1998 | |
|---|---|---|---|---|
| | Cost | Fair Value | Cost | Fair Value |
| Foreign Public Equity Pools | | | | |
| Multi-region | $ 14,606 | $ 17,102 | $ 13,109 | $ 15,606 |
| Europe | 11,001 | 12,621 | 8,805 | 11,958 |
| Pacific basin | 7,252 | 8,222 | 7,903 | 6,425 |
| Emerging markets | 569 | 808 | - | - |
| | 33,428 | 38,753 | 29,817 | 33,989 |
| United States | 5,640 | 10,041 | 4,439 | 7,458 |
| Canadian Public Equity Pools | | | | |
| Large capitalized companies | 8,071 | 7,924 | - | - |
| Small capitalized companies | 9,268 | 9,610 | 9,461 | 11,864 |
| | 17,339 | 17,534 | 9,461 | 11,864 |
| Total - Alberta Heritage Scholarship Fund | $ 56,407 | $ 66,328 | $ 43,717 | $ 53,311 |
| Total - External Managers Fund (a)(b) | $ 3,537,698 | $ 4,338,781 | $ 2,399,553 | $ 3,043,960 |

(a) The Fund is managed by external managers with expertise in global equity markets and Canadian small capitalized companies and large capitalized companies. The objective of the Fund is to provide investment returns higher than the total return of the applicable Morgan Stanley, Standard and Poor's and Toronto Stock Exchange indices over a four year period. The portfolio is comprised of publicly traded equity securities on Canadian and approved foreign markets. Risk is reduced through manager, style and market diversification.

(b) The following is a summary of assets and liabilities of the External Managers Fund as at March 31, 1999.

| | 1999 | 1998 |
|---|---|---|
| | ($ thousands) | |
| Cash and short-term securities | $ 109,079 | $ 130,426 |
| Investments | | |
| Public equities | 3,438,393 | 2,270,812 |
| Fixed-income securities | 1,247 | 3,936 |
| Accrued interest and accounts receivable | 27,890 | 27,357 |
| Accounts payable | (38,641) | (32,978) |
| Total - External Managers Fund | $ 3,537,968 | $ 2,399,553 |

ALBERTA RISK MANAGEMENT FUND
FINANCIAL STATEMENTS
MARCH 31, 1999



## AUDITOR'S REPORT

To the Provincial Treasurer

I have audited the balance sheet of the Alberta Risk Management Fund as at March 31, 1999 and the statement of operations for the year then ended. These financial statements are the responsibility of the Fund's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In my opinion, these financial statements present fairly, in all material respects, the financial position of the Fund as at March 31, 1999 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles.

Peter Valentine, FCA
Auditor General

Edmonton, Alberta
May 26, 1999

## ALBERTA RISK MANAGEMENT FUND
## BALANCE SHEET
## AS AT MARCH 31, 1999

| | 1999 | 1998 |
|---|---|---|
| **ASSETS** | | |
| Cash (Note 3) | $ 9,752,245 | $ 2,017,789 |
| Accounts receivable (Note 4) | 95,434 | 386,654 |
| | $ 9,847,679 | $ 2,404,443 |
| **LIABILITIES AND DEFICIT** | | |
| Accounts payable (Note 5) | $ 11,295,528 | $ 11,011,262 |
| Deficit | (1,447,849) | (8,606,819) |
| | $ 9,847,679 | $ 2,404,443 |

The accompanying notes are part of these financial statements.

## ALBERTA RISK MANAGEMENT FUND
## STATEMENT OF OPERATIONS
## FOR THE YEAR ENDED MARCH 31, 1999

| | 1999 | | 1998 |
|---|---|---|---|
| | Budget | Actual | Actual |
| Income | | | |
| Insurance services | | | |
| Province of Alberta departments, funds and agencies | $ 11,273,000 | $ 12,284,159 | $ 6,520,502 |
| Other | 634,000 | 106,866 | 337,417 |
| Interest | 337,000 | 529,095 | 150,175 |
| | 12,244,000 | 12,920,120 | 7,008,094 |
| Expenses | | | |
| Insurance claims, premiums and other services | 5,351,000 | 5,088,316 | 8,834,688 |
| Administration | 689,000 | 672,834 | 673,369 |
| | 6,040,000 | 5,761,150 | 9,508,057 |
| Net income (loss) | $ 6,204,000 | 7,158,970 | (2,499,963) |
| Deficit at beginning of year | | 8,606,819 | 6,106,856 |
| Deficit at end of year | | $ 1,447,849 | $ 8,606,819 |

The accompanying notes are part of these financial statements.

# ALBERTA RISK MANAGEMENT FUND
## NOTES TO THE FINANCIAL STATEMENTS
## MARCH 31, 1999

Note 1 Authority and Purpose

The Alberta Risk Management Fund (the Fund) operates under the authority of the Financial Administration Act, Chapter F-9, Revised Statutes of Alberta 1980, as amended.

The Fund facilitates the provision of risk management and insurance services to government departments and other entities within the Alberta Government by assuming general and automobile liability and the risk of property and other losses in exchange for premiums related to the level of risk assumed.

Note 2 Significant Accounting Policies and Reporting Practices

These financial statements are prepared in accordance with generally accepted accounting principles. The accounting policies of significance to the Fund are as follows:

(a) Claims provisions, including provisions for claims incurred but not reported, are based on estimates made by management. The provisions are adjusted in the period when more experience is acquired and as additional information is obtained.

(b) Estimates are used in accruing revenues and expenses in circumstances where the actual accrued revenues and expenses are unknown at the time the financial statements are prepared. Uncertainty in the determination of the amount at which an item is recognized in financial statements is known as measurement uncertainty. Such uncertainty exists when there is a variance between the recognized amount and another reasonably possible amount, as there is whenever estimates are used.

Measurement uncertainty that is material to these financial statements exists in the accrual of claims provisions. The nature of the uncertainty in these items arises from several factors such as the effect of claims incurred but not reported and estimates of claims payable.

(c) The fair values of cash, accounts receivable and payable are estimated to approximate their book values.

(d) A statement of changes in financial position is not provided as disclosure in these financial statements is considered adequate.

Note 3 Cash

Cash consists of deposits in the Consolidated Cash Investment Trust Fund which is managed with the objective of providing competitive interest income to depositors while maintaining maximum security and liquidity of depositors' capital. The portfolio is comprised of high quality short-term and long-term fixed income securities with a maximum term to maturity of five years.

Note 4 Accounts Receivable

Accounts receivable consists of the following:

| | 1999 | 1998 |
|---|---|---|
| Estimated claims recoverable | $ 61,437 | $ 161,485 |
| Receivable from Province of Alberta departments, funds and agencies | 25,530 | 22,918 |
| Other | 8,467 | 202,251 |
| | $ 95,434 | $ 386,654 |

Note 5 Accounts Payable

Accounts payable consists of the following:

| | 1999 | 1998 |
|---|---|---|
| Estimated claims payable | $ 11,115,426 | $ 10,800,275 |
| Payable to the Treasury Department - Administration costs | 177,008 | 193,150 |
| Other | 3,094 | 17,837 |
| | $ 11,295,528 | $ 11,011,262 |

Note 6 Contingent Liabilities

At March 31, 1999, the Province was named as defendant in various legal actions relating to insurance claims. The resulting loss if any from these claims and other potential claims cannot be determined.

Note 7 Uncertainty Due to the Year 2000

The year 2000 issue is the result of some computer systems using two digits rather than four to define the applicable year. Government computer systems that have date sensitive software may recognize a date using "00" as the year 1900 rather than the year 2000, which could result in miscalculations or system failures. In addition, similar problems may arise in some systems if certain dates in 1999 are not recognized as a valid date or are recognized to represent something other than a date. The effects of the year 2000 issue may be experienced before, on, or after January 1, 2000. If not addressed, the effect on operations and financial reporting may range from minor errors to significant systems failure that could affect the ability to conduct some operations. Despite the government's efforts to address this issue, it is not possible to be certain that all aspects of the year 2000 issue affecting the Fund, including those related to the efforts of customers, suppliers and other third parties, will be fully resolved.

Note 8 Approval of Financial Statements

These financial statements were approved by management.

# UTILITY COMPANIES INCOME TAX REBATES FUND
# FINANCIAL STATEMENT
# MARCH 31, 1999



## AUDITOR'S REPORT

To the Provincial Treasurer

I have audited the balance sheet of the Utility Companies Income Tax Rebates Fund as at March 31, 1999. This financial statement is the responsibility of the Fund's management. My responsibility is to express an opinion on this financial statement based on my audit.

I conducted my audit in accordance with generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statement is free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statement. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In my opinion, this financial statement presents fairly, in all material respects, the financial position of the Fund as at March 31, 1999 in accordance with generally accepted accounting principles.

Peter Valentine, FCA
Auditor General

Edmonton, Alberta
June 30, 1999

# UTILITY COMPANIES INCOME TAX REBATES FUND
## BALANCE SHEET
## MARCH 31,1999

| | 1999 | 1998 |
|---|---|---|
| **ASSETS** | | |
| Cash | $ 1,371,724 | $ 589,831 |
| Accounts receivable | 9,215 | 456,101 |
| | $ 1,380,939 | $ 1,045,932 |
| **LIABILITIES** | | |
| Accounts payable | $ 1,380,939 | $ 1,045,932 |

The accompanying notes are part of this financial statement.

# UTILITY COMPANIES INCOME TAX REBATES FUND
## NOTES TO THE FINANCIAL STATEMENT
## MARCH 31, 1999

Note 1 Authority and Purpose

The Utility Companies Income Tax Rebates Fund (the Fund) operates under the authority of the Utility Companies Income Tax Rebates Act, Chapter U-10, Revised Statutes of Alberta 1980, as amended.

The Fund makes payments to utility companies in Alberta for the benefit of their customers from money transferred by the Government of Canada under the Public Utilities Income Tax Transfer Act (Canada).

Note 2 Cessation of Operations

The Fund ceased normal operations in 1996-97, due to the termination of transfers by the Government of Canada. However, the Fund continues to process adjustments of prior year taxes.

During the year, the Fund discharged $923,428 of prior year liabilities to Government of Canada and $48,927 to utility companies and rural gas co-ops. In addition, the Fund received $1,298,147 of transfer adjustments from the Government of Canada and $9,215 previous year rebates from utility companies and rural gas co-ops. Liabilities as a result of the recovery will be discharged in 1999-2000.

Note 3 Investment Income

Investment income of the Fund is credited directly to the Department of Treasury.

Note 4 Approval of Financial Statement

This financial statement was approved by management.

ALBERTA INSURANCE COUNCIL
FINANCIAL STATEMENTS
DECEMBER 31, 1998



## AUDITORS' REPORT

To the Members of the Alberta Insurance Council

We have audited the balance sheet of Alberta Insurance Council as at December 31, 1998 and the statements of revenue, expenditures and operating and changes in financial position for the year then ended. These financial statements are the responsibility of the Council's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Council as at December 31, 1998 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles.

PricewaterhouseCoopers LLP
Chartered Accountants

Edmonton, Alberta
March 12, 1999

## ALBERTA INSURANCE COUNCIL
## BALANCE SHEET
## AS AT DECEMBER 31, 1998

| | 1998 | 1997 |
|---|---|---|
| **ASSETS** | | |
| Current assets | | |
| Cash | $ 1,464,923 | $ 1,416,463 |
| Accounts receivable | 1,893 | 2,396 |
| Prepaid expenses | 4,973 | 5,468 |
| | 1,471,789 | 1,424,327 |
| Capital assets (Note 4) | 168,388 | 136,787 |
| | $ 1,640,177 | $ 1,561,114 |
| **LIABILITIES** | | |
| Current liabilities | | |
| Accounts payable | $ 46,006 | $ 44,827 |
| Deferred licence and assessment fee revenue (Note 2) | 283,498 | 298,609 |
| | 329,504 | 343,436 |
| **EQUITY IN NET ASSETS** | | |
| Net assets | 1,310,673 | 1,217,678 |
| | $ 1,640,177 | $ 1,561,114 |

ALBERTA INSURANCE COUNCIL
STATEMENT OF REVENUE AND EXPENDITURES
FOR THE YEAR ENDED DECEMBER 31, 1998

| | Budget 1998 | 1998 | 1997 |
|---|---|---|---|
| Revenue | | | |
| Licence and exam fees (Note 2) | $ 1,280,000 | $ 1,459,630 | $ 1,245,112 |
| Interest and other | 50,000 | 76,376 | 50,352 |
| | 1,330,000 | 1,536,006 | 1,295,464 |
| Expenditures | | | |
| Salaries and benefits | 770,000 | 785,323 | 703,553 |
| Council meetings | 165,000 | 123,096 | 95,325 |
| Appeal boards | 45,000 | 21,301 | - |
| Occupancy | 109,000 | 90,755 | 92,357 |
| Freight and postage | 60,000 | 59,993 | 48,392 |
| Printing and stationery | 55,000 | 40,332 | 28,115 |
| Office | 25,000 | 15,220 | 9,657 |
| Travel | 100,000 | 59,018 | 47,054 |
| Communications | 45,000 | 29,156 | 33,479 |
| Professional fees | 45,000 | 69,523 | 110,958 |
| Amortization of capital assets | - | 86,972 | 68,892 |
| Software maintenance | 20,000 | 16,439 | 11,428 |
| Insurance | 11,000 | 5,571 | 18,409 |
| Promotions and publications | 15,000 | 5,640 | 20,243 |
| Legal fees | 15,000 | 15,816 | 2,219 |
| Other | - | 18,856 | 16,502 |
| | 1,480,000 | 1,443,011 | 1,306,583 |
| Excess (deficiency) revenue over expenditures for the year | | 92,995 | (11,119) |
| Net assets - Beginning of year | | | |
| As previously stated | | 1,217,678 | 1,416,908 |
| Cumulative adjustment resulting from accounting change (Note 7) | | - | (188,111) |
| As restated | | 1,217,678 | 1,228,797 |
| Net assets - End of year | | $ 1,310,673 | $ 1,217,678 |

## ALBERTA INSURANCE COUNCIL
## STATEMENT OF CHANGES IN FINANCIAL POSITION
## FOR THE YEAR ENDED DECEMBER 31, 1998

| | 1998 | 1997 |
|---|---|---|
| Operating activities | | |
| Net revenue (expenditures) for the year | $ 92,995 | $ (11,119) |
| Item not affecting cash | | |
| Amortization of capital assets | 86,972 | 68,892 |
| | 179,967 | 57,773 |
| Net changes in non-cash working capital items | | |
| Decrease (increase) in accounts receivable | 503 | (1,701) |
| Decrease in prepaid expenses | 495 | 1,327 |
| Increase in accounts payable | 1,179 | 24,448 |
| Decrease in due to the Province of Alberta | - | (10,330) |
| Increase (decrease) in deferred licence revenue | (15,111) | 110,498 |
| | 167,033 | 182,015 |
| Investing activities | | |
| Purchase of capital assets | (118,573) | (18,566) |
| Proceeds from sale of capital assets | - | 374 |
| | (118,573) | (18,192) |
| Increase in cash | 48,460 | 163,823 |
| Cash - Beginning of year | 1,416,463 | 1,252,640 |
| Cash - End of year | $ 1,464,923 | $ 1,416,463 |

## ALBERTA INSURANCE COUNCIL
## NOTES TO FINANCIAL STATEMENTS
## DECEMBER 31, 1998

Note 1 Authority and purpose

The Alberta Insurance Council operates under the authority of the Insurance Act, Chapter I-5, Revised Statutes of Alberta 1980, as amended.

The Alberta Insurance Council provides administration services to the Life Insurance, General Insurance and Insurance Adjusters Councils. These Councils are responsible for regulating their segments of the insurance industry.

Note 2 Summary of significant accounting policies

These financial statements have been prepared by management in accordance with accounting principles generally accepted in Canada. Because the precise determination of many assets, liabilities revenues and expenses are dependent upon future events, the preparation of financial statements for a period necessarily includes the use of estimates and approximations which have been made using careful judgement. Actual results could differ from those estimates. These financial statements have, in management's opinion, been properly prepared within reasonable limits of materiality and within the framework of the accounting policies summarized below.

Revenue recognition

License and assessment fees are taken into income on a straight line basis over the term of the license or assessment. License and assessment fees received but not yet taken into income are recorded as deferred license and assessment fee revenue. Examination fees are taken into income when the related exam is held.

Until April 2, 1997, pursuant to the delegation of certain licensing and administrative functions to it by the Superintendent of Insurance, the Council collected prescribed licensing and examination fees which it remitted to the Provincial Treasurer. In return, the Council received from the General Revenue Fund of the Province of Alberta an amount equal to 85% of the fees collected. This arrangement ended in April, 1997, and from that time, the Council retains all license and exam fees collected which are recorded as revenue in accordance with the revenue recognition policy described above.

Capital assets and amortization

Capital assets are recorded at cost and are amortized over their estimated useful lives on a straight-line basis as follows:

| | |
|---|---|
| Leasehold improvements | term of lease |
| Furniture and office equipment | 10 years |
| Computer equipment | 3 years |
| Computer software | 3 years |
| Telephone equipment | 5 years |

Note 3 Cash

Included in Cash is an amount of $1,348,776 (1997 - $1,291,784) invested in the Consolidated Cash Investment Trust Fund ("CCITF"). The CCITF is being managed with the objective of providing competitive interest income to depositors while maintaining maximum security and liquidity of depositors' capital. The portfolio is comprised of high-quality short-term and mid-term fixed income securities with a maximum term to maturity of five years.

Note 4 Capital assets

| | 1998 | | | 1997 |
|---|---|---|---|---|
| | Cost | Accumulated amortization | Net | Net |
| Leasehold improvements | $ 44,511 | $ 12,923 | $ 31,588 | $ - |
| Furniture and office equipment | 122,714 | 68,716 | 53,998 | 42,581 |
| Computer equipment | 136,193 | 109,836 | 26,357 | 43,151 |
| Computer software | 107,655 | 56,628 | 51,027 | 48,407 |
| Telephone equipment | 15,204 | 9,786 | 5,418 | 2,648 |
| | $ 426,277 | $ 257,889 | $ 168,388 | $ 136,787 |

Note 5 Lease commitments

The Council is committed to operating leases payments for business premises and equipment as follows:

| | |
|---|---|
| 1999 | $ 89,955 |
| 2000 | $ 59,058 |

Subsequent to year end, the Council entered into negotiations with its landlord to extend its lease terms on its Edmonton location until the year 2006.

Note 6 Financial instruments

The carrying value of financial assets and liabilities approximate fair value. The Council does not hedge interest rate or foreign currency transactions, and there are no unrecorded financial instruments. Credit risk is negligible as the majority of revenue is from license, assessment and examination fees which are billed in advance.

Note 7 Accounting changes

In 1997, the Council retroactively adopted a policy to recognize license fee revenue over the term of the license. Previously, license fees were recognized as revenue when received. This accounting change had the effect of reducing opening net assets in 1996 by $11,400 and reducing the net revenue for the year in 1996 by $23,289. The 1997 opening retained earnings have been restated to reflect this change.

Note 8 Uncertainty due to the Year 2000 Issue

The Year 2000 Issue arises because many computerized systems use two digits rather than four to identify a year. Date-sensitive systems may recognize the year 2000 as 1900 or some other date, resulting in errors when information using year 2000 dates is processed. In addition, similar problems may arise in some systems which use certain dates in 1999 to represent something other than a date. The effects of the Year 2000 Issue may be experienced before, on, or after January 1, 2000, and, if not addressed, the impact on operations and financial reporting may range from minor errors to significant systems failure which could affect the Council's ability to conduct normal business operations. It is not possible to be certain that all aspects of the Year 2000 Issue affecting the Council, including those related to the efforts of members, customers, suppliers, or other third parties, will be fully resolved.

Schedule 1

## ALBERTA INSURANCE COUNCIL
## SCHEDULE OF SALARIES AND BENEFITS
## FOR THE YEAR ENDED DECEMBER 31, 1998

### PER DIEM PAYMENTS TO COUNCIL MEMBERS

| | 1998 | | 1997 | |
|---|---|---|---|---|
| | # | Total | # | Total |
| Councils (a) | | | | |
| Chairs | 4 | $ 20,100 | 4 | $ 21,000 |
| Council Members | 19 | 56,500 | 19 | 45,100 |
| Total | 23 | $ 76,600 | 23 | $ 66,100 |

(a) This includes the Alberta Insurance Council, the Life Insurance Council, the General Insurance Council and the Insurance Adjusters Council.

### SALARIES AND BENEFITS

| | 1998 | | | | 1997 | |
|---|---|---|---|---|---|---|
| | # | Salary [b] | Benefits [c] | Total | # | Total |
| General Manager | 1 | $ 100,417 | $ 19,618 | $ 120,035 | 1 | $ 100,720 |
| Assistant General Manager | 1 | 74,205 | 13,425 | 87,630 | 1 | 73,379 |
| Full-time staff [d] | 14 | 502,930 | 71,487 | 574,417 | 13 | 522,866 |
| Part-time staff | 3 | 2,815 | 426 | 3,241 | 2 | 6,588 |
| Total | 19 | $ 680,367 | $ 104,956 | $ 785,323 | 17 | $ 703,553 |

(b) Salary includes regular base pay, bonuses, overtime and accrued vacation pay. Accrued vacation pay was $3,839 for 1998 and $3,535 for 1997.

(c) Employer's share of all employee benefits and contributions or payments made on behalf of employees including group RRSP, health care, dental coverage, group life insurance and long and short term disability plans.

(d) Full-time staff consists of all individuals working 29 hours or more per week. Average annual salary was $42,389 for 1998 and $40,449 for 1997.

ALBERTA MUNICIPAL FINANCING CORPORATION
FINANCIAL STATEMENTS
DECEMBER 31, 1998



## AUDITOR'S REPORT

To the Shareholders of the
Alberta Municipal Financing Corporation

I have audited the balance sheet of the Alberta Municipal Financing Corporation as at December 31, 1998 and the statements of income and retained earnings and changes in financial position for the year then ended. These financial statements are the responsibility of the Corporation's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In my opinion, these financial statements present fairly, in all material respects, the financial position of the Corporation as at December 31, 1998 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles.

Peter Valentine, FCA
Auditor General

Edmonton, Alberta
January 29, 1999

## ALBERTA MUNICIPAL FINANCING CORPORATION
## BALANCE SHEET
## AS AT DECEMBER 31, 1998
(thousands of dollars)

| | 1998 Budget | 1998 Actual | 1997 Actual |
|---|---|---|---|
| **ASSETS** | | | |
| Cash (Note 3) | $ 228,873 | $ 246,052 | $ 179,779 |
| Short-term investments | - | 39,348 | - |
| Accrued interest receivable | 162,472 | 158,884 | 176,871 |
| Loans to local authorities (Note 4) | 3,769,987 | 3,716,178 | 4,082,664 |
| Sinking fund assets (Note 5 and Schedule 1) | 419,804 | 417,639 | 385,304 |
| | $ 4,581,136 | $ 4,578,101 | $ 4,824,618 |
| **LIABILITIES AND SHAREHOLDERS' EQUITY** | | | |
| Liabilities: | | | |
| Accrued interest payable | $ 85,069 | $ 85,217 | $ 91,004 |
| Long-term debt (Note 6 and Schedule 2) | 4,174,218 | 4,174,218 | 4,400,045 |
| | 4,259,287 | 4,259,435 | 4,491,049 |
| Shareholders' equity: | | | |
| Share capital (Note 7): | | | |
| Authorized: 7,500 common shares, par value $10 per share | | | |
| Issued and fully paid: 6,367 shares (1997 - 6,371) | 64 | 64 | 64 |
| Retained earnings | 321,785 | 318,602 | 333,505 |
| | 321,849 | 318,666 | 333,569 |
| | $ 4,581,136 | $ 4,578,101 | $ 4,824,618 |

A.J. McPherson
President and Chairman of the Board

G. H. Sherwin
Vice-President

The accompanying notes are part of these financial statements.

# ALBERTA MUNICIPAL FINANCING CORPORATION
## STATEMENT OF INCOME AND RETAINED EARNINGS
## FOR THE YEAR ENDED DECEMBER 31, 1998

(thousands of dollars)

| | 1998 | | 1997 |
|---|---|---|---|
| | Budget | Actual | Actual |
| Interest Income | | | |
| Loans | $ 422,475 | $ 417,622 | $ 467,270 |
| Amortization of loan discounts | 36,134 | 36,133 | 42,859 |
| Deposits and short-term investments | 8,200 | 12,378 | 2,967 |
| | 466,809 | 466,133 | 513,096 |
| Interest Expense | | | |
| Debt | 510,390 | 510,390 | 526,355 |
| Amortization of long-term debt discounts | 818 | 818 | 858 |
| | 511,208 | 511,208 | 527,213 |
| Net interest expense | (44,399) | (45,075) | (14,117) |
| Other Income | | | |
| Investment income on sinking fund assets | 30,000 | 27,835 | 35,040 |
| Loan prepayment fees | 3,000 | 2,649 | 653 |
| | 33,000 | 30,484 | 35,693 |
| Net (expense) interest and other income | (11,399) | (14,591) | 21,576 |
| Non-Interest Expense | | | |
| Administration and office expenses (Note 8) | 258 | 256 | 231 |
| Debt issue and service expenses | 43 | 38 | 39 |
| Directors' and officers' fees and expenses (Note 8) | 20 | 18 | 12 |
| | 321 | 312 | 282 |
| Net (loss) income | (11,720) | (14,903) | 21,294 |
| Retained earnings, beginning of year | 333,505 | 333,505 | 312,211 |
| Retained earnings, end of year | $ 321,785 | $ 318,602 | $ 333,505 |

## ALBERTA MUNICIPAL FINANCING CORPORATION
## STATEMENT OF CHANGES IN FINANCIAL POSITION
## FOR THE YEAR ENDED DECEMBER 31, 1998

(thousands of dollars)

| | 1998 | | 1997 |
|---|---|---|---|
| | Budget | Actual | Actual |
| Operating transactions: | | | |
| Net (loss) income | $ (11,720) | $ (14,903) | $ 21,294 |
| Add (deduct) non-cash items: | | | |
| Decrease in accrued interest, net | 8,464 | 12,200 | 8,482 |
| Amortization of loan discounts | (36,134) | (36,133) | (42,859) |
| Amortization of premiums and discounts on sinking fund investments | (28,324) | (27,796) | (28,324) |
| Amortization of long-term debt discounts | 818 | 818 | 858 |
| Cash applied to operating transactions | (66,896) | (65,814) | (40,549) |
| Investing transactions: | | | |
| Short-term investments | - | (39,348) | - |
| Loan repayments | 563,811 | 562,723 | 495,961 |
| New loans | (215,000) | (160,104) | (164,624) |
| Cash provided by investing transactions | 348,811 | 363,271 | 331,337 |
| Financing trasactions: | | | |
| Increase in sinking fund assets, net | (6,176) | (4,539) | (11,216) |
| Redemption of long-term debt | (226,645) | (226,645) | (175,457) |
| Cash applied to financing transactions | (232,821) | (231,184) | (186,673) |
| Increase in cash | 49,094 | 66,273 | 104,115 |
| Cash at beginning of year | 179,779 | 179,779 | 75,664 |
| Cash at end of year | $ 228,873 | $ 246,052 | $ 179,779 |

## ALBERTA MUNICIPAL FINANCING CORPORATION
## NOTES TO THE FINANCIAL STATEMENTS
## DECEMBER 31, 1998

Note 1 Authority

The Alberta Municipal Financing Corporation operates under the authority of the Alberta Municipal Financing Corporation Act, Chapter A-33, Revised Statutes of Alberta 1980, as amended.

Note 2 Significant Accounting Policies and Reporting Practices

(a) Short-term Investments

Short-term investments are recorded at cost or amortized cost, adjusted to recognize other than temporary losses in the underlying values. All securities held were purchased with the intention to hold them to maturity. Gains and losses on disposal of short-term investments are included in the year of disposal.

(b) Sinking Fund Investments

Sinking fund investments are recorded at cost. The cost includes the amount of applicable amortization of discount or premium using the straight-line method over the life of the investments.

Realized gains and losses on disposals of sinking fund investments are included in the determination of investment income. The cost of disposals is determined on the average cost basis.

Where there has been a loss in value of an investment that is other than a temporary decline, the investment is written down to recognize the loss. The written down value is deemed to be the new cost.

Investment income on sinking fund investments accrues to the sinking fund.

(c) Long-term Debt

Long-term debt discounts, including underwriting commission, arising on the issue of long-term debt are deferred and amortized over the term of the long-term debt.

Long-term debt is recorded net of unamortized discounts.

Public long-term debt issue expenses are charged against income as they are incurred.

(d) Discounts on Loans to Local Authorities

Discounts are recorded for reductions of interest rates given on loans to local authorities with interest rates above a certain level and are amortized to income over the term of these loans. Annual amortization is the change in the present value of the remaining interest rate reduction.

## Note 3 Cash

Cash consists of deposits in the Consolidated Cash Investment Trust Fund (CCITF) of the Province of Alberta. CCITF is being managed with the objective of providing competitive interest income to depositors while maintaining maximum security and liquidity of depositors' capital. The portfolio is comprised of high-quality short-term and mid-term fixed income securities with a maximum term to maturity of five years. Interest is earned on the Fund's daily cash balance at the average rate of interest earned by CCITF, which varies depending on prevailing market interest rates.

## Note 4 Loans to Local Authorities

| | 1998 | 1997 |
|---|---|---|
| | (thousands of dollars) | |
| Loans to local authorities | $ 3,842,396 | $ 4,245,015 |
| Less: Unamortized discounts | 126,218 | 162,351 |
| | $ 3,716,178 | $ 4,082,664 |

## Note 5 Sinking Fund Assets

Sinking fund assets relate to the $450,000,000 December 15, 2002 public issue of long-term debt.

## Note 6 Long-term Debt

(a) The long-term debt of the Corporation is fully guaranteed by the Province of Alberta.

(b) Long-term debt amounting to $3,316,761,000 (1997 - $3,493,406,000) held by the Canada Pension Plan Investment Fund is redeemable at the option of the Minister of Finance of Canada by giving six months notice in writing and observing the other redemption provisions of the long-term debt agreement.

(c) Sinking fund and long-term debt redemption requirements during each of the next five years are as follows:

| | Sinking Fund | Long-term Debt Redemption | Total |
|---|---|---|---|
| | | (thousands of dollars) | |
| 1999 | $ 4,500 | $ 294,206 | 298,706 |
| 2000 | 4,500 | 442,367 | 446,867 |
| 2001 | 4,500 | 331,739 | 336,239 |
| 2002 | 4,500 | 724,735 | 729,235 |
| 2003 | - | 441,023 | 441,023 |
| | $ 18,000 | $ 2,234,070 | $ 2,252,070 |

Note 7 Share Capital

Particulars of share capital are summarized hereunder:

| | | Number of Shares | | |
|---|---|---|---|---|
| Class | Restricted to | Authorized | Issued and Fully Paid | Total Dollar Amount |
| A | Province of Alberta | 4,500 | 4,500 | $ 45,000 |
| B | Municipalities and hospitals | 1,000 | 846 | 8,460 |
| C | Cities | 750 | 577 | 5,770 |
| D | Towns and villages | 750 | 312 | 3,120 |
| E | Schools, universities and colleges | 500 | 132 | 1,320 |
| | | 7,500 | 6,367 | $ 63,670 |

During the year, 2 Class B, 7 Class D and 1 Class E shares were issued and 7 Class B, 3 Class C, 3 Class D and 1 Class E shares were cancelled at $10.00 each.

Note 8 Directors' Fees and Related Party Transactions

Directors' fees paid by the Corporation are as follows:

| | 1998 | | 1997 | |
|---|---|---|---|---|
| | Number of Individuals | Total | Number of Individuals | Total |
| Chairman of the Board | 1 | $ 1,400 | 1 | $ 1,200 |
| Board members | 8 | $ 8,100 | 8 | $ 5,600 |

Two of the Board members are employees of the Province of Alberta and do not receive compensation from the Corporation.

The Corporation has no employees. Administration and office expenses of $219,945 (1997 - $195,624) were paid to the controlling shareholder, Province of Alberta, at prices which approximate market.

## Note 9 Interest Rate Risk

Interest rate risk refers to the potential impact of changes in interest rates on the Corporation's earnings and the fair value of the financial instruments when maturities of its financial assets are not matched with the maturities of its financial debt. The following table shows the maturities and effective rates of the Corporation's financial assets and liabilities:

As at December 31, 1998
(thousands of dollars)

| Maturities | Within 1 Year | 1 to 2 Years | 3 to 5 Years | 5 to 10 Years | Over 10 Years | Total |
|---|---|---|---|---|---|---|
| Assets | | | | | | |
| Cash | $246,052 | | | | | $ 246,052 |
| Effective rate | 5.0% | | | | | |
| Accrued interest receivable | 158,884 | | | | | 158,884 |
| Investments | 39,348 | | | | | 39,348 |
| Effective rate | 5.8% | | | | | |
| Loans | 37,124 | 66,680 | 850,017 | 1,620,706 | 1,267,869 | 3,842,396 |
| Effective rate | 10.3% | 11.3% | 9.9% | 11.0% | 9.1% | 10.1% |
| Sinking fund | | | 417,639 | | | 417,639 |
| Effective rate | | | 8.9% | | | |
| Total | 481,408 | 66,680 | 1,267,656 | 1,620,706 | 1,267,869 | 4,704,319 |
| Liabilities | | | | | | |
| Accrued interest payable | 85,217 | - | - | - | - | 85,217 |
| Debt | 294,201 | 442,367 | 1,494,959 | 1,612,168 | 330,523 | 4,174,218 (1) |
| Effective rate | 10.4% | 12.5% | 13.7% | 10.9% | 9.9% | 12.0% |
| Total | 379,418 | 442,367 | 1,494,959 | 1,612,168 | 330,523 | 4,259,435 |
| Net gap | $ 101,990 | $ (375,687) | $ (227,303) | $ 8,538 | $ 937,346 | $ 444,884 |

(1) This total is not reduced by unamortized discount of $126,218.

The Corporation manages on a continuous basis its interest rate risk by matching its debt maturity profile to the forecast cash flows and their effect on the Corporation's surplus position. Based on the maturity of its current outstanding loans and debt, the Corporation is able to repay its debt from cash flows without additional borrowing for the next five years.

## Note 10 Fair Value of Financial Instruments

The amounts set out in the table represent the fair value of the Corporation's financial instruments based on the following assumptions and valuation methods.

Fair value represents the Corporation's estimate of amounts for cash, short-term investments, sinking fund assets and debt that could be exchanged with unrelated parties who are interested in acquiring these instruments. For loans which lack an available trading market, fair value is based on estimates using net present value techniques which reflect the Corporation's lending rates.

The fair value of accrued interest receivables and payables approximate their carrying value.

Interest rate sensitivity is the main cause of changes in the fair value of the Corporation's financial instruments.

| | 1998 | | 1997 | |
|---|---|---|---|---|
| | Fair Value | Book Value | Fair Value | Book Value |
| | (thousands of dollars) | | | |
| Assets | | | | |
| Cash | $ 246,052 | $ 246,052 | $ 179,779 | $ 179,779 |
| Short-term investments | 39,562 | 39,348 | - | - |
| Sinking fund assets | 429,454 | 417,639 | 399,348 | 385,304 |
| Loans | 4,676,713 | 3,716,178 | 5,151,581 | 4,082,664 |
| Liabilities | | | | |
| Debt | 5,291,530 | 4,174,218 | 5,578,251 | 4,400,045 |

Note 11 Uncertainty Due to the Year 2000 Issue

The year 2000 issue arises because many computerized systems use two digits rather than four to identify a year. Date sensitive systems may recognize the year 2000 as 1900 or some other date, resulting in errors when information using the year 2000 is processed. In addition, similar problems may arise in some systems which use certain dates in 1999 to represent something other than the date. The effects of the year 2000 issue may be experienced before, on or after January 1, 2000, and, if not addressed, the impact on operations and financial reporting may range from minor errors to significant system failures. Even when management devotes time and effort to assessing the effects of the year 2000 issue and implementing a year 2000 plan, as is the case with the Corporation it is not possible to be sure that all aspects of the year 2000 issue affecting the entity, including those related to the efforts of customers, suppliers, and other third parties, will be fully resolved in time.

Note 12 Budget

The 1998 budget was approved by the Board of Directors on April 24, 1998.

Schedule 1

## ALBERTA MUNICIPAL FINANCING CORPORATION
## SCHEDULE OF SINKING FUND ASSETS
## AS AT DECEMBER 31, 1998

(thousands of dollars)

| | Book Value | Market Value |
|---|---|---|
| Investments | | |
| Bonds and debentures: | | |
| Corporate | $ 49,129 | $ 48,974 |
| Bond coupons and residuals: | | |
| Government of Canada, direct | 135,491 | 138,330 |
| Provincial, direct: | | |
| Alberta Municipal Financing Corporation | 207,595 | 216,043 |
| Other | 16,471 | 17,028 |
| Bond coupons and residuals - short-term: | | |
| Provincial, direct: | | |
| Alberta Municipal Financing Corporation | 8,946 | 9,072 |
| Total | 417,632 | 429,447 |
| Cash | 7 | 7 |
| Total 1998 | $ 417,639 | $ 429,454 |
| Total 1997 | $ 385,304 | $ 399,348 |

# ALBERTA MUNICIPAL FINANCING CORPORATION
## SCHEDULE OF LONG-TERM DEBT
## AS AT DECEMBER 31, 1998

(thousands of dollars)

| Date of Issue | Maturity Date | Interest Rate | Principal Outstanding |
|---|---|---|---|
| Province of Alberta | | | |
| Nov 01, 1979 | Nov 01, 1999 | 11.70 | $ 70,000 |
| Mar 03, 1980 | Mar 03, 2000 | 13.45 | 35,000 |
| Aug 15, 1980 | Aug 15, 2000 | 13.20 | 35,000 |
| Total | | | 140,000 |
| Canada Pension Plan Investment Fund (Note 6(b)) | | | |
| Nov 15, 1979 | Oct 01, 1999 | 10.04 | 219,206 |
| Nov 14, 1980 | Oct 01, 2000 | 12.35 | 222,367 |
| Sep 15, 1981 | Aug 01, 2001 | 14.18 | 216,739 |
| Jun 01, 1982 | Jun 01, 2002 | 15.75 | 274,735 |
| Apr 05, 1983 | Apr 05, 2003 | 13.82 | 209,284 |
| Dec 01, 1983 | Dec 01, 2003 | 11.50 | 231,739 |
| Dec 03, 1984 | Dec 03, 2004 | 13.25 | 338,491 |
| Nov 01, 1985 | Nov 01, 2005 | 11.66 | 283,604 |
| Nov 03, 1986 | Nov 03, 2006 | 9.85 | 395,396 |
| Nov 02, 1987 | Nov 02, 2007 | 9.66 | 335,383 |
| Oct 03, 1988 | Oct 03, 2008 | 10.04 | 259,294 |
| Oct 02, 1989 | Oct 02, 2009 | 9.99 | 291,414 |
| Nov 01, 1989 | Nov 01, 2009 | 9.62 | 32,457 |
| Dec 01, 1989 | Dec 01, 2009 | 9.26 | 6,652 |
| Total | | | 3,316,761 |
| Public | | | |
| Dec 17, 1979 | Dec 15, 2000 | 11.85 | 70,000 |
| Jul 02, 1980 | Jul 03, 2000 | 11.75 | 30,000 |
| Dec 01, 1980 | Dec 01, 2000 | 13.65 | 50,000 |
| Mar 02, 1981 | Mar 02, 2001 | 14.10 | 30,000 |
| Jun 15, 1981 | Jun 15, 2001 | 16.25 | 85,000 |
| Jan 18, 1983 | *Dec 15, 2002 | 12.25 | 450,000 |
| Mar 23, 1994 | Mar 23, 1999 | 6.25 | 1,000 |
| Mar 23, 1994 | Mar 23, 1999 | 6.25 | 4,000 |
| Total | | | 720,000 |
| | | | 4,176,761 |
| Less: Unamortized long-term debt discount | | | 2,543 |
| Total long-term debt | | | $ 4,174,218 |

*AMFC has the right to redeem the debentures of this issue in whole but not in part on December 15, 2000 or any interest payment date thereafter prior to maturity.

ALBERTA PENSIONS ADMINISTRATION CORPORATION
FINANCIAL STATEMENTS
DECEMBER 31, 1998



## AUDITOR'S REPORT

To the Shareholder of Alberta Pensions Administration Corporation

I have audited the balance sheet of the Alberta Pensions Administration Corporation as at December 31, 1998 and the statements of income and cash flows for the year then ended. These financial statements are the responsibility of the Corporation's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In my opinion, these financial statements present fairly, in all material respects, the financial position of the Corporation as at December 31, 1998 and the results of its operations and its cash flows for the year then ended in accordance with generally accepted accounting principles.

Peter Valentine, FCA
Auditor General

Edmonton, Alberta
March 12, 1999

# ALBERTA PENSIONS ADMINISTRATION CORPORATION
## BALANCE SHEET
## AS AT DECEMBER 31, 1998

| | 1998 | 1997 |
|---|---|---|
| **ASSETS** | | |
| Current: | | |
| Cash (Note 4) | $ 116,013 | $ 117,924 |
| Accounts receivable | 77,161 | 25,888 |
| Due from pension plans | 1,491,764 | 1,042,595 |
| | 1,684,938 | 1,186,407 |
| Capital assets (Note 5) | 396,417 | 1,764,867 |
| | $ 2,081,355 | $ 2,951,274 |
| **LIABILITIES AND SHAREHOLDER'S EQUITY** | | |
| Current: | | |
| Accounts payable and accrued liabilities | $ 841,539 | $ 712,849 |
| Accrued salaries and benefits | 378,398 | 439,410 |
| Accrued pension liability (Note 12) | 290,000 | 27,794 |
| Accrued vacation pay | 175,000 | 6,353 |
| Unearned capital contributions (Note 3(b)) | 128,535 | 555,481 |
| | 1,813,472 | 1,741,887 |
| Unearned capital contributions (Note 3(b)) | 267,882 | 1,209,386 |
| | 2,081,354 | 2,951,273 |
| Shareholder's equity: | | |
| Share capital (Note 6) | 1 | 1 |
| | $ 2,081,355 | $ 2,951,274 |

On behalf of the Board:

Jack H. McMahon
Chairman of the Board

Allan J. Habstritt
Audit Committee Chairman

The accompanying notes are part of these financial statements.

# ALBERTA PENSIONS ADMINISTRATION CORPORATION
## STATEMENT OF INCOME
## FOR THE YEAR ENDED DECEMBER 31, 1998

| | Budget 1998 (Note 16) | Actual 1998 | Actual 1997 |
|---|---|---|---|
| Revenue | | | |
| Service revenue (Note 7) | $ 10,907,000 | $ 11,563,343 | $ 8,901,773 |
| Miscellaneous revenue (Note 8) | 115,000 | 237,296 | 31,528 |
| Total revenue | 11,022,000 | 11,800,639 | 8,933,301 |
| Operating costs before Business Process Reengineering (BPR) and plan specific costs | | | |
| Salaries and benefits | 5,385,000 | 5,314,080 | 4,714,773 |
| Data processing | 1,385,000 | 1,698,553 | 889,857 |
| Amortization of capital assets | 298,000 | 184,566 | 322,953 |
| Contract services | 785,000 | 462,406 | 454,721 |
| Materials and supplies | 700,000 | 566,175 | 551,718 |
| Rent | 496,000 | 450,122 | 475,434 |
| Operating costs before BPR and plan specific costs | 9,049,000 | 8,675,902 | 7,409,456 |
| BPR operating costs | | | |
| Salaries and benefits | - | 266,396 | - |
| Amortization of capital assets (Note 5) | 373,000 | 1,412,737 | 372,723 |
| Contract services | - | 283,948 | - |
| BPR operating costs | 373,000 | 1,963,081 | 372,723 |
| Operating costs before plan specific costs | 9,422,000 | 10,638,983 | 7,782,179 |
| Plan specific costs (Note 10) | 1,600,000 | 1,161,656 | 1,151,122 |
| Total operating costs | 11,022,000 | 11,800,639 | 8,933,301 |
| Net income | $ - | $ - | $ - |

## ALBERTA PENSIONS ADMINISTRATION CORPORATION
## STATEMENT OF CASH FLOWS
## FOR THE YEAR ENDED DECEMBER 31, 1998

| | 1998 | 1997 |
|---|---|---|
| Operating activities | | |
| Net income | $ - | $ - |
| Items not requiring cash | | |
| Amortization | 1,597,303 | 695,676 |
| Gain on disposal of capital assets | (2,932) | - |
| Capital contributions recognized in current year | (1,597,303) | (695,676) |
| | (2,932) | - |
| Changes in non-cash working capital | | |
| Increase in accounts receivable | (51,273) | (19,692) |
| Increase (decrease) in due from pension plans | (449,169) | 276,210 |
| Increase (decrease) in accounts payable and accrued liabilities | 128,690 | (8,495) |
| Decrease in accrued salaries and benefits | (61,012) | (198,416) |
| Increase in unfunded pension liability | 262,206 | 27,794 |
| Increase in vacation pay | 168,647 | 6,353 |
| | (4,843) | 83,754 |
| Investing activities | | |
| Proceeds on sale of capital assets | 8,425 | - |
| Acquisition of capital assets | (234,346) | (891,069) |
| | (225,921) | (891,069) |
| Financing activities | | |
| Increase in capital contributions | 228,853 | 891,069 |
| (Decrease) increase in cash for the year | (1,911) | 83,754 |
| Cash at beginning of year | 117,924 | 34,170 |
| Cash at end of year | $ 116,013 | $ 117,924 |

ALBERTA PENSIONS ADMINISTRATION CORPORATION
NOTES TO THE FINANCIAL STATEMENTS
DECEMBER 31, 1998

Note 1 Authority

The Alberta Pensions Administration Corporation (APA) was incorporated on August 10, 1995 under the Business Corporation Act, Chapter B-15, Statutes of Alberta, and commenced operations on November 1, 1995. The issued share of the Corporation is owned by the Province of Alberta, and accordingly the Corporation is exempt from income taxes.

Note 2 Nature of Operations

The Provincial Treasurer of Alberta, operating under the authority of the Public Sector Pension Plans Act, Chapter P-30.7, Statutes of Alberta 1993, as amended, is responsible for administering several Alberta public sector pension plans. On November 1, 1995, the Provincial Treasurer transferred all of the pension administration operations, including all related computer hardware, computer software, office furniture and equipment to the Corporation.

By agreement dated November 1, 1995, between the Provincial Treasurer, as administrator of the pension plans, and the Corporation, the Corporation is to provide administrative services, on a cost recovery basis, for the period November 1, 1995 through March 31, 1999 to the following pension plans:

The Local Authorities Pension Plan
The Public Service Pension Plan
The Universities Academic Pension Plan
The Management Employees Pension Plan
The Special Forces Pension Plan
The Public Service Management (Closed Membership) Pension Plan
The Provincial Judges and Masters In Chambers Pension Plan
The Members of the Legislative Assembly Pension Plan

The Provincial Treasurer and the Corporation have agreed to extend the provisions of this agreement to December 31, 2001.

All administrative services required by the pension plans are provided by the Corporation. These services include the collection of contributions, payment of benefits and refunds, communication to stakeholders, pension plan board support services and other services specifically approved by individual pension boards.

Note 3 Significant Accounting Policy

(a) Capital Assets

Capital assets are recorded at cost

Capital assets are amortized on a straight line basis over the estimated useful life of the asset as follows:

| | |
|---|---|
| Computer equipment | 2 to 3 years |
| Computer software | 2 to 3 years |
| Furniture and equipment | 5 years |
| Telephone system | 3 years |
| Leasehold improvements | Lease period |
| Business process reengineering (BPR) | 5 years |

The costs of business process reengineering activities directly attributable to the development, betterment or acquisition of computer software are capitalized. These activities include:

Costs associated with defining plan rules and developing specifications for programming new pension software.

Purchase and installation of new pension software.

Program modifications to new pension software.

Capital assets under construction, including software development projects, are not amortized until completion and implementation.

(b) Revenue Recognition

Contributions to acquire capital assets are recorded as unearned capital contributions. These amounts are recognized as revenue on the same basis as the acquired capital assets are amortized to operating costs.

Note 4 Cash

Cash consists of deposits in the Consolidated Cash Investment Trust Fund of the Province of Alberta. The Fund is invested primarily in securities maturing in less than one year which are either issued or guaranteed by the Canadian federal and provincial governments, deposits given by or guaranteed by chartered banks, or short-term investment-grade-quality notes of Canadian corporations. Interest is earned on the daily cash balance at the average rate of earnings of the Fund which varies depending on prevailing market interest rates. Interest earned on deposits is included in miscellaneous revenue.

Note 5 Capital Assets

| | 1998 | | | 1997 |
|---|---|---|---|---|
| | Cost | Accumulated Amortization | Net Book Value | Net Book Value |
| Computer equipment | $ 485,710 | $ 363,335 | $ 122,375 | $ 251,399 |
| Software development projects | 203,307 | 191,892 | 11,415 | 31,058 |
| Computer software | 154,314 | 153,365 | 949 | 4,585 |
| Furniture and equipment | 64,798 | 18,431 | 46,367 | 29,043 |
| Telephone system | 42,515 | 29,524 | 12,991 | 27,162 |
| Leasehold improvements | 9,179 | 2,073 | 7,106 | 8,883 |
| Technology reengineering [1] | - | - | - | 1,412,737 |
| Business process reengineering | 195,214 | - | 195,214 | - |
| | $ 1,155,037 | $ 758,620 | $ 396,417 | $ 1,764,867 |

(1) The Corporation adopted, on a prospective basis, a new accounting policy with respect to the treatment of costs on its technology re-engineering project. Costs totaling $1,412,737 that have been capitalized in prior years were fully amortized and written off in 1998.

The change in accounting policy resulted in amortization for 1998 increasing from $557,289 to $1,597,303.

Note 6 Share Capital

| | 1998 | 1997 |
|---|---|---|
| Authorized | | |
| Unlimited number of common shares | | |
| Unlimited number of preferred shares | | |
| Issued | | |
| 1 common share, for cash | $1 | $1 |

Note 7 Service Revenue

The Corporation charged each pension plan with its respective share of the Corporation's operating costs less miscellaneous revenue.

| | 1998 | 1997 |
|---|---|---|
| The Local Authorities Pension Plan | $ 6,376,312 | $ 5,001,095 |
| The Public Service Pension Plan | 3,446,659 | 2,453,719 |
| The Universities Academic Pension Plan | 660,902 | 501,879 |
| The Management Employees Pension Plan | 440,664 | 412,968 |
| The Special Forces Pension Plan | 370,862 | 319,352 |
| The Public Service Management (Closed Membership) Pension Plan | 147,660 | 104,463 |
| The Provincial Judges and Masters in Chambers Pension Plan | 61,642 | 55,658 |
| The Members of the Legislative Assembly Pension Plan | 58,642 | 52,639 |
| Total Service Revenue | $ 11,563,343 | $ 8,901,773 |

Note 8 Miscellaneous revenue

| | 1998 | 1997 |
|---|---|---|
| Miscellaneous revenue is comprised of: | | |
| Cost recovery from Telus | $ 124,020 | $ 13,306 |
| Cost recovery from pension plans | 83,000 | - |
| Interest | 26,530 | 14,823 |
| Other | 3,746 | 3,399 |
| | $ 237,296 | $ 31,528 |

Note 9 Related Party Transactions

The Corporation received the following services at amounts which approximate market from:

| | | 1998 | 1997 |
|---|---|---|---|
| Alberta Treasury | Accounting and administrative | $ 98,656 | $ 98,120 |
| | Staffing services | 3,359,686 | 4,846,799 |
| Alberta Public Works, Supply & Services | Data processing, postage and office space | 530,354 | 707,161 |
| Auditor General of Alberta | Auditing - Corporation | 13,400 | 11,000 |
| | Auditing - pension plans | 135,250 | 123,400 |
| PSC Payment Systems Corporation | Payroll and pension benefits processing | 42,432 | 52,216 |

The Corporation also provided services to the Provincial Pension Plans as disclosed in Note 7.

Note 10 Plan Specific Costs

The Corporation makes certain payments on behalf of the pension plans. These costs, which are incurred directly by the pension plans, and which the Corporation does not control, are as follows:

| | 1998 | 1997 |
|---|---|---|
| Pension board remuneration | $ 168,144 | $ 187,293 |
| Contract services | 685,508 | 695,777 |
| Materials and supplies | 308,004 | 268,052 |
| | $ 1,161,656 | $ 1,151,122 |

## Note 11 Salaries and Benefits

| | 1998 | | | | 1997 | |
|---|---|---|---|---|---|---|
| | Number of Individuals | Salary[1] | Benefits and Allowances | Total | Number of Individuals | Total |
| Chairman of APA Board | 1 | $ 3,000 | $ - | $ 3,000 | 1 | $ 3,000 |
| Board Members of APA[(3)] | 3 | 6,000 | - | 6,000 | 3 | 6,000 |
| Executives: | | | | | | |
| Chief Operating Officer | 1 | 116,641 | 14,188 | 130,829 | 1 | 95,856 |
| Director Finance and Administration | 1 | 90,956 | 13,744 | 104,700 | 1 | 97,424 |
| Director Business Transformation | 1 | 89,848 | 13,222 | 103,070 | | - |
| Director Operations | 1 | 88,649 | 12,974 | 101,623 | 1 | 77,877 |
| Secretary Pension Board | 1 | 75,335 | 12,116 | 87,451 | 1 | 82,128 |

Salaries include regular base pay, honoraria and other direct cash remuneration.

Benefits and allowances include employer's share of benefits provided, including pensions, health care, dental, group life insurance, long-term disability benefits, workers' compensation, payments in lieu of vacation earned but not taken and professional memberships.

Remuneration paid to the Chairman and Board Members is classified as contract services.

## Note 12 Pension Liability

During the year, employees of the Corporation participated in the Public Service Pension Plan and the Management Employees Pension Plan. The Corporation's portion of the unfunded liability for pre-1992 pensionable service for these two plans is $290,000 (1997: $27,794). The liability was determined by actuarial valuations as at December 31, 1997 extrapolated to December 31, 1998. The 1997 comparative was only for the Management Employees Pension Plan based on an actuarial valuation as at December 31, 1996 extrapolated to December 31, 1997.

The actuarial valuations used the projected benefit method prorated on service. Assumptions used in the valuations are based on the pension boards' best estimate of future events. The plans' future experience will inevitably vary, perhaps significantly, from the assumptions. Differences between the actuarial assumptions and future experience will emerge as gains or losses in future valuations and will be amortized over the expected average remaining service life of the employee group.

The Public Sector Pension Plans Act specifies the basis to determine the amount of the total unfunded liability for each plan which will be funded by employers, employees and Government. APA's liability is based on its percentage of the total pensionable payroll of all employers in each plan.

## Note 13 Uncertainty Due to the Year 2000

The year 2000 issue is the result of some computer programs being written using two digits rather than four to define the applicable year. Computer programs that have date sensitive software may recognize a date using "00" as the year 1900 rather than the year 2000, which could result in miscalculations or system failures. In addition, similar problems may arise in some systems if certain dates in 1999 are not recognized as a valid date or are recognized to represent something other than a date. The effects of the year 2000 issue may be experienced before, on, or after January 1, 2000. If not addressed, the effect on operations and financial reporting may range from minor errors to significant systems failure that could affect the ability to conduct some operations.

Management is currently working to resolve the potential effect of the year 2000 on the processing of date sensitive information by the Corporation's computerized information systems in a timely manner. Despite efforts to address this issue, it is not possible to be certain that all aspects of the year 2000 issue affecting the Corporation, including those related to the efforts of customers, suppliers and other third parties, will be fully resolved.

Note 14 Commitments

The Corporation has entered into agreements with minimum annual commitments as follows:

As assignee in the lease agreement between the Landlord and Alberta Public Works, Supply and Services for office space.

| | |
|---|---|
| 1999 to 2002 | $495,000 |

An agreement with a service provider for the provision of pension payroll services to August 31, 2000.

| | |
|---|---|
| 1999 | $164,000 |
| 2000 | $117,000 |

An agreement with a service provider for the provision of information technology services commencing September 1, 1998 to August 31, 2003.

| | |
|---|---|
| 1999 | $1,077,000 |
| 2000 | $ 951,000 |
| 2001 | $ 817,000 |
| 2002 | $ 798,000 |
| 2003 | $ 532,000 |

An agreement with a service provider for the lease of hardware and software for local area network, production server and desktop computer equipment. This agreement covers a three year term commencing January 1, 1999.

| | |
|---|---|
| 1999 to 2001 | |
| Operating lease | $149,000 |
| Capital leases | $ 88,000 |

Note 15 Subsequent Events

The Corporation has entered into agreements with a software provider for the purchase and implementation of financial and accounting software totaling $80,000 in 1999.

The Corporation has entered into an agreement in principle with a software provider for pension software to meet future technology reengineering requirements. The two year agreement is valued at $1,600,000.

The Corporation entered into an agreement until March 31, 1999 with Alberta Treasury for the provision of staffing services on a cost basis. These staff became employees of APA on February 4, 1999 resulting in the Corporation assuming responsibility for the earned vacation and unfunded pension liabilities of approximately $250,000 and $114,000 respectively.

Note 16 Budget

The 1998 budget was approved by the Board of Directors on January 21, 1998.

Note 17 Comparative Figures

Comparative figures have been restated to be consistent with the 1998 presentation.

ALBERTA SECURITIES COMMISSION
FINANCIAL STATEMENTS
MARCH 31, 1999



## AUDITOR'S REPORT

To the Members of the Alberta Securities Commission

I have audited the balance sheet of the Alberta Securities Commission as at March 31, 1999 and the statements of revenue, expense and retained earnings, and cash flows for the year then ended. These financial statements are the responsibility of the Commission's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In my opinion, these financial statements present fairly, in all material respects, the financial position of the Commission as at March 31, 1999 and the results of its operations and the changes in its cash flows for the year then ended in accordance with generally accepted accounting principles.

Peter Valentine, FCA
Auditor General

Edmonton, Alberta
May 3, 1999

# ALBERTA SECURITIES COMMISSION
## BALANCE SHEET
## AS AT MARCH 31, 1999

(with comparative figures as at March 31, 1998)

| | 1999 | 1998 |
|---|---|---|
| **ASSETS** | | |
| Current | | |
| Cash (Note 3) | $ 2,649,030 | $ 13,757,215 |
| Accounts receivable | 175,912 | 219,369 |
| Work-in-progress | 50,540 | 58,471 |
| Prepaid Expense | 21,080 | - |
| | 2,896,562 | 14,035,055 |
| Investments (Note 4) | 14,445,050 | - |
| Capital assets (Note 5) | 1,082,713 | 1,095,001 |
| Total assets | $ 18,424,325 | $ 15,130,056 |
| **LIABILITIES AND RETAINED EARNINGS** | | |
| Current | | |
| Accounts payable and accrued liabilities | $ 1,135,194 | $ 526,648 |
| Unearned revenue | 308,568 | 511,941 |
| Current portion of lease inducement | 40,158 | 40,158 |
| | 1,483,920 | 1,078,747 |
| Lease inducement (Note 6) | 40,158 | 80,316 |
| Unfunded pension (Note 7) | 82,650 | 77,562 |
| Total liabilities | 1,606,728 | 1,236,625 |
| Retained earnings | 16,817,597 | 13,893,431 |
| Total liabilities and retained earnings | $ 18,424,325 | $ 15,130,056 |

Approved on behalf of the Members

W. L. Hess, Q.C. , Chair

Ian E. W. McConnan, FCA, Member

The accompanying notes and schedule are part of these financial statements.

## ALBERTA SECURITIES COMMISSION
## STATEMENT OF REVENUE, EXPENSE AND RETAINED EARNINGS
## FOR THE YEAR ENDED MARCH 31, 1999

(with comparative figures for the year ended March 31, 1998)

| | 1999 | | 1998 |
|---|---|---|---|
| | Budget (Note 9) | Actual | Actual |
| REVENUE | | | |
| Fees | $ 8,939,000 | $ 11,481,868 | $ 11,200,447 |
| Investment income | 724,000 | 1,248,811 | 482,191 |
| Administrative settlements | 350,000 | 363,737 | 364,520 |
| Other | 93,000 | 64,599 | 77,874 |
| | 10,106,000 | 13,159,015 | 12,125,032 |
| EXPENSE | | | |
| Salaries and benefits (Schedule 1) | 6,351,577 | 6,207,493 | 5,075,744 |
| Premises | 513,000 | 501,125 | 409,300 |
| Materials and supplies | 356,300 | 374,463 | 410,736 |
| Contribution-Alberta Capital Market Foundation | 1,002,000 | 1,160,353 | - |
| Contract services | 833,500 | 616,772 | 896,853 |
| Travel | 373,280 | 400,165 | 321,069 |
| Amortization | 265,000 | 267,379 | 240,233 |
| Telephone and communicaitons | 169,400 | 140,848 | 140,644 |
| Member fees (Schedule 1) | 238,000 | 116,050 | 76,512 |
| Other | 321,350 | 312,282 | 308,336 |
| Loss on disposal of capital assets | - | 137,919 | 2,006 |
| Total expense | 10,423,407 | 10,234,849 | 7,881,433 |
| Net income (loss) | (317,407) | 2,924,166 | 4,243,599 |
| Retained earnings at beginning of year | 13,893,431 | 13,893,431 | 9,649,832 |
| Retained earnings at end of year | $ 13,576,024 | $ 16,817,597 | $ 13,893,431 |

The accompanying notes and schedule are part of these financial statements.

## ALBERTA SECURITIES COMMISSION
## STATEMENT OF CASH FLOWS
## FOR THE YEAR ENDED MARCH 31, 1999

(with comparative figures for the year ended March 31, 1998)

| | 1999 | 1998 |
|---|---|---|
| Cash provided by operations | | |
| Net income | $ 2,924,166 | $ 4,243,599 |
| Amortization, net | 227,221 | 200,075 |
| Loss on disposal of capital assets | 137,919 | 2,006 |
| Increase (reduction) of unfunded pension | 5,088 | (58,184) |
| | 3,294,394 | 4,387,496 |
| Changes in non-cash working capital items relating to operations | | |
| Accounts receivable | 43,457 | (57,579) |
| Work-in-progress and prepaid expenses | (13,149) | (15,161) |
| Accounts payable and accrued liabilities | 608,546 | 7,595 |
| Unearned revenue | (203,373) | (165,581) |
| | 435,481 | (230,726) |
| Cash from operations | 3,729,875 | 4,156,770 |
| Cash Used in Investing Activities | | |
| Investments | (14,445,050) | - |
| Purchase of capital assets | (393,010) | (544,966) |
| | (14,838,060) | (544,966) |
| Change in cash during the year | (11,108,185) | 3,611,804 |
| Cash at beginning of the year | 13,757,215 | 10,145,411 |
| Cash at end of the year | $ 2,649,030 | $ 13,757,215 |

The accompanying notes and schedule are part of these financial statements.

ALBERTA SECURITIES COMMISSION
NOTES TO THE FINANCIAL STATEMENTS
MARCH 31, 1999

Note 1 Nature of Operations

The Alberta Securities Commission (the "Commission") is a Provincial Corporation under the Securities Act (Alberta) (the "Act"). The business of the Commission is the regulation of the Alberta Capital Market, including the administration of the Act, the Securities Regulation and the Alberta Securities Commission Rules.

The mission of the Commission is to foster a fair and efficient capital market in Alberta and confidence in that market. In carrying out its mission the Commission strives to balance the needs of investors for adequate protection with the needs of industry to access capital necessary for continued economic growth.

Note 2 Significant Accounting Policies

(a) Valuation of Investments

Fixed income securities held by the Commission through the Canadian Dollar Public Debt Pool are recorded at cost. Cost includes the amount of applicable amortization of discount or premium using the straight line method over the life of the investments.

Where there has been a decline in value in an investment that is other than a temporary decline, the investment is written down to recognize the loss. The written down value is deemed to be the new cost.

(b) Capital Assets

Capital assets are recorded at cost. The Commission capitalizes labour and out of pocket costs for significant individual systems development projects. Assets are amortized on a straight line basis over their estimated useful lives as follows:

| | |
|---|---|
| Computer equipment | 3 years |
| Furniture and equipment | 10 years |
| Systems development costs | 5 years |
| Leasehold improvements | from 3.5 years to 10 years |

(c) Revenue Recognition

Fees are recognized as revenue when the relevant order, receipt, certificate or other acknowledgement is issued. Fees received concerning matters in progress at year end are recorded as unearned revenue and an estimate of labour costs on these matters is recorded as work in progress. Cost recoveries from Commission Orders and Settlement Agreements are recognized as revenues when cash is received. Investment income is recorded on the accrual basis. Gains and losses arising as a result of disposals are included in the determination of investment income.

(d) Pension Costs

Pension costs and recoveries are included in salaries and benefits. Pension costs and recoveries comprise: the cost of pension benefits earned by employees during the year; interest on the Commission's share of the unfunded pension amount; the amortization of deferred adjustments over the expected average remaining service life of employees which relate to the long term; adjustments to the pension obligation recognized immediately if there is reasonable assurance that a gain or loss has been realized; and the effect of the change in the ratio used to allocate the plan's total unfunded amount to participating entities.

(e) Lease Inducement

Cash payments received as lease inducements are deferred and amortized on a straight line basis over the lease term.

(f) Fair Value

(i) The carrying value of cash, receivables and payables, and accruals approximate their fair value due to the relatively short periods to maturity of the instruments.

(ii) The fair value of investments as disclosed in Note 4 is market value. Public fixed income securities are valued at the period-end closing sale price or the average of the latest bid and ask prices quoted by an independent securities valuation company.

(g) Derivative Financial Investments

Income and expense on index swaps and interest rate swaps are accrued as earned and included in investment income. As explained in Note 4(b) controls are in place respecting the use of derivatives.

Note 3 Cash

Daily bank balances are maintained in the Consolidated Cash Investment Trust Fund. The Consolidated Cash Investment Trust Fund is administered by the Provincial Treasurer with the objective of providing competitive interest income to depositors while maintaining maximum security and liquidity of depositor's capital. The portfolio is comprised of high quality short-term and mid-term fixed income securities with a maximum term to maturity of five years.

Note 4 Investments

The Commission's investments are held in the Canadian Dollar Public Debt Pool ("CDPDP"), a pooled investment fund established and administered by the Provincial Treasurer. Pooled investment funds have a market based value that is used to allocate income to participants and to value purchases and sales of pool units.

CDPDP is managed with the objective of providing competitive returns compared to the total return of the Scotia Macleod Universe Bond Index over a four year period while maintaining maximum security and liquidity of participants' capital. The portfolio is comprised of high quality Canadian fixed income instruments and debt related derivatives. Competitive returns are achieved through management of the portfolio duration and sector rotation. Securities held by CDPDP at March 31, 1999 have an average effective yield of 5.51% per annum based on market. As at March 31, 1999, the securities have the following term structure based on par: under 1 year - 10%; 1 to 5 years – 37%; 5 to 10 years – 24%; 10 to 20 years – 21%; over 20 years – 8%.

(a) Investment Risk Management

Income and financial returns of the Commission are exposed to credit risk and price risk. Credit risk relates to the possibility that a loss may occur from the failure of another party to perform according to the terms of a contract. Price risk is comprised of interest rate risk and market risk. Interest rate risk relates to the possibility that the investments will change in value due to fluctuations in market interest rates. Market risk relates to the possibility that the investments will change in value due to future fluctuations in market prices.

In order to earn an optimal financial return at an acceptable level of risk, management of the Commission has established an investment policy which will be reviewed annually. Risk is reduced through the investment in a pooled debt fund with sufficient diversification and quality restraints on fixed income investments. Individual investments in non-listed and foreign securities are not eligible investments outside of CDPDP. CDPDP uses derivative securities to enhance returns.

(b) Index and Interest Rate Swaps

CDPDP uses index and interest rate swaps to enhance return and for hedging risks. A swap is a contractual agreement between two parties to exchange a series of cash flows based on a notional amount and does not involve the exchange of the underlying principal.

An index swap involves the exchange of a floating interest rate cash flow for one based on the performance of a market index. For interest rate swaps, parties generally exchange fixed and floating rate interest cash flows based on a notional value. Notional value is the amount to which a rate or price is applied in order to calculate the exchange of cash flows. All swaps are supported by underlying securities. Leveraging is not permitted.

The Commission's proportionate share of the notional value of index and interest rate swaps issued by CDPDP as at March 31, 1999 are as follows: Bond index swaps - $2,672,433; Interest rate swaps - $1,920,592.

The fair value of swaps have been included in the determination of the fair value of the pooled investment.

(c) Summary

The following is a summary of the Commission's investment in the CDPDP as at March 31, 1999.

| | Cost | Fair Value |
|---|---|---|
| Deposit in the Consolidated Cash Investment Trust Fund | $ 200,678 | $ 200,678 |
| Public fixed-income securities | | |
| Government of Canada, direct and guaranteed | 3,895,457 | 3,916,249 |
| Province of Alberta, direct and guaranteed | 329,073 | 339,287 |
| Other provinces, direct and guaranteed | 1,802,330 | 1,857,746 |
| Municipal | 147,016 | 145,537 |
| Corporate | 5,824,129 | 5,636,934 |
| Private fixed-income securities | | |
| Corporate | 2,074,741 | 1,975,639 |
| Total deposit and fixed-income securities | 14,273,424 | 14,072,070 |
| Accrued interest and accounts receivable | 346,928 | 346,928 |
| Accounts Payable | (175,302) | (175,302) |
| | 171,626 | 171,626 |
| Total - Alberta Securities Commission | $ 14,445,050 | $ 14,243,696 |
| Total - Canadian Dollar Public Debt Pool | $ 7,812,035,000 | $ 8,112,618,000 |

(d) Investment Returns

The CDPDP pool uses the time-weighted rate of return based on market values to measure performance. The measure involves the calculation of the return realized by the pool over a specified period and is a measure of the total proceeds received from an investment dollar initially invested. Total proceeds include cash distributions (interest and dividend payments) and gains or losses (realized and unrealized).

The time-weighted rate of return measures the compounded rate of growth of the initial investment over the specified period. It is designed to eliminate the effect that the size and timing of cash flows have on the internal rate of return. The investment industry uses time-weighted rates of return calculated using market values when comparing the return of pools with other pools or indices.

The Commission has been a participant in CDPDP from May 1, 1998 to March 31, 1999. The Commission's rate of return for its investment in CDPDP for eleven months was 6.68%. On an annualized basis the Commission's rate of return for its investment in CDPDP for eleven months was 7.31%. This compares to the Scotia Macleod Universe Bond Index annualized rate of return of 6.99% for the year ended March 31, 1999.

Note 5 Capital Assets

| | 1999 | | | 1998 |
|---|---|---|---|---|
| | Cost | Accumulated Amortization | Net Book Value | Net Book Value |
| Computer equipment | $ 676,448 | $ 419,566 | $ 256,882 | $ 235,990 |
| Furniture and equipment | 422,461 | 111,389 | 311,072 | 275,101 |
| Systems development costs | 110,021 | 82,516 | 27,505 | 49,510 |
| Leasehold improvements | 578,229 | 90,975 | 487,254 | 534,400 |
| | $ 1,787,159 | $ 704,446 | $ 1,082,713 | $ 1,095,001 |

Note 6 Lease Inducement

Pursuant to a ten year lease agreement effective April 1, 1996 the Commission received from its landlord a lease inducement of $199,645 and is entitled to a further $199,645 at the beginning of year six. Amortization for each year is $40,158.

Note 7 Unfunded Pension

The Commission's share of the Public Service Pension Plan pension obligation for pre – 1992 pensionable service as at March 31, 1999 is \$82,650 (1998 \$77,562). The amount was determined by actuarial valuation as at December 31, 1997 extrapolated to March 31, 1999.

The actuarial valuation used the projected benefit method prorated on service. Assumptions used in the valuation are based on the Pension Board's best estimate of future events. The Plan's future experience will inevitably vary, perhaps significantly, from the assumptions. Differences between the actuarial assumptions and future experience will emerge as gains or losses and will be amortized over the expected average remaining service life of the employee group.

The Public Sector Pension Plans Act specifies the basis to determine the amount of the total unfunded amount for each pension plan that will be funded by employers and employees. The Commission's portion of its liabilities is based on the Commission's percentage of the total pensionable payroll of all employers in the pension plan.

Note 8 Lease Obligations

Future minimum operating lease payments for premises and equipment for each of the next 5 years and in aggregate are as follows:

| | |
|---|---|
| 2000 | \$ 633,976 |
| 2001 | 637,616 |
| 2002 | 690,181 |
| 2003 | 616,104 |
| 2004 | 602,399 |
| Thereafter | 1,211,030 |
| Total | \$ 4,391,306 |

Note 9 Budget

The members approved the Commission's 1998-99 budget on January 21, 1998 with a subsequent revision and approval on July 8, 1998. The original budget was increased by \$130,000. This amount is reflected in the budget included with these financial statements.

Note 10 Contingencies

(a) The Commission is involved in various legal proceedings arising from its regulatory activities. Management considers the chance of liability under these legal proceedings not to be determinable and accordingly an estimate of any contingent loss cannot be made.

(b) The Commission, along with the Ontario Securities Commission and the British Columbia Securities Commission entered into a Continuing Guarantee Agreement, to guarantee the liabilities of the Mutual Fund Dealers Association of Canada with a Canadian Chartered Bank. The obligation of the Commission to the Bank is limited to \$2,160,000.

Note 11 The Year 2000

The year 2000 issue is the result of some computer systems using two digits rather than four to define the applicable year. Computer systems that have date sensitive software may recognize a date using "00" as the year 1900 rather than the year 2000, which could result in miscalculations or system failures. In addition, similar problems may arise in some systems if certain dates in 1999 are not recognized as a valid date or are recognized to represent something other than a date. The effects of the year 2000 issue may be experienced before, on, or after January 1, 2000. If not addressed, the effect on operations and financial reporting may range from minor errors to significant systems failure that could affect the ability to conduct some Commission operations. Despite the Commission's efforts to address this issue, it is not possible to be certain that all aspects of the year 2000 issue affecting the Commission, including those related to the efforts of customers, suppliers and other third parties, will be fully resolved

Note 12 Related Party Transactions

Travel service arrangements provided by a Member's travel agency, including fees for airlines tickets - \$53,451.

These services are provided in the normal course of operations and are measured at fair value for the services provided.

Note 13 Comparative Figures

The comparative figures are for the year ended March 31, 1998. Certain 1998 figures have been reclassified where necessary to conform to 1999 presentation.

Schedule 1

# ALBERTA SECURITIES COMMISSION
# SCHEDULE OF SALARIES AND BENEFITS
# FOR THE YEAR ENDED MARCH 31, 1999

(with comparative figures for the year ended March 31, 1998)

| | 1999 | | | | 1998 | |
|---|---|---|---|---|---|---|
| | Number of Individuals (1) | Salary (2) | Benefits and Allowances (3) | Total | Number of Individuals (1) | Total |
| Securities Commission Members (part-time) | 6.5 | $ 116,050 | $ - | $ 116,050 | 6.5 | $ 76,512 |
| Chair, Securities Commission (4) | 1 | $ 275,000 | $ 15,466 | $ 290,466 | 1 | $ 269,559 |
| Vice Chair, Securities Commission (4) | 1 | 130,000 | 8,864 | 138,864 | 0.5 | 67,177 |
| Executive Director | 1 | 140,000 | 13,025 | 153,025 | 1 | 115,230 |
| Chief Financial Officer | 1 | 120,000 | 8,874 | 128,874 | 1 | 134,783 |
| Director, Capital Markets | 1 | 110,000 | 9,133 | 119,133 | 1 | 99,192 |

(1) Number of individuals is the weighted average during the year.

(2) Salary includes regular base pay, bonuses, overtime and lump sum payments and honoraria.

(3) Employer's share of all employee benefits and contributions or payments made on behalf of employees including health care, dental coverage, out of country medical benefits, group life insurance, accidental disability and dismemberment insurance, long and short term disability plan, vacation payouts, professional memberships, tuition, and club memberships.

(4) The Chair and Vice-Chair are full time Commission Members.

# THE ALBERTA GOVERNMENT TELEPHONES COMMISSION
# CONSOLIDATED FINANCIAL STATEMENTS
# DECEMBER 31, 1998



## AUDITOR'S REPORT

To the Members of
The Alberta Government Telephones Commission

I have audited the consolidated balance sheet of The Alberta Government Telephones Commission as at December 31, 1998 and the consolidated statements of revenue, expense and retained earnings and cash flows for the year then ended. These financial statements are the responsibility of the Commission's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In my opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Commission as at December 31, 1998 and the results of its operations and its cash flows for the year then ended in accordance with generally accepted accounting principles.

Peter Valentine, FCA
Auditor General

Edmonton, Alberta
February 20, 1999

THE ALBERTA GOVERNMENT TELEPHONES COMMISSION
CONSOLIDATED BALANCE SHEET
AS AT DECEMBER 31, 1998
(thousands of dollars)

| | 1998 | 1997 |
|---|---|---|
| **ASSETS** | | |
| Cash and cash equivalents (Note 3) | $ 103,033 | $ 92,460 |
| Interest and accounts receivable | 3,188 | 13,283 |
| Notes receivable (Note 4) | 200,000 | 400,000 |
| Loans receivable | - | 424 |
| Property held for sale | - | 1,470 |
| | $ 306,221 | $ 507,637 |
| **LIABILITIES AND EQUITY** | | |
| Bank overdraft | $ - | $ 2,766 |
| Accounts payable and accrued liabilities | 2,994 | 12,925 |
| Income taxes (Note 2(d)) | 37,067 | 33,048 |
| Debenture debt (Note 5) | 200,000 | 400,000 |
| Due to the Province of Alberta (Note 6) | 65,096 | 57,921 |
| | 305,157 | 506,660 |
| Equity: | | |
| Retained earnings | - | - |
| Foreign currency translation adjustments (Note 7) | 1,064 | 977 |
| | $ 306,221 | $ 507,637 |

On behalf of the Commission:
Robert Bhatia
Chairman and Commission Member

Peter McNeil
Commission Member

The accompanying notes are part of these consolidated financial statements.

## THE ALBERTA GOVERNMENT TELEPHONES COMMISSION
## CONSOLIDATED STATEMENT OF REVENUE, EXPENSE AND RETAINED EARNINGS
## FOR THE YEAR ENDED DECEMBER 31, 1998

(thousands of dollars)

| | 1998 Budget (Note 12) | 1998 Actual | 1997 |
|---|---|---|---|
| Revenue: | | | |
| Interest on notes receivable | $ 32,989 | $ 32,989 | $ 52,804 |
| Interest premium (Note 4) | 909 | 909 | 1,533 |
| Earn-out (Note 10) | 5,520 | 5,520 | 480 |
| Interest on deposits | 191 | 173 | 80 |
| | 39,609 | 39,591 | 54,897 |
| Expense: | | | |
| Interest on debenture debt | 32,989 | 32,989 | 52,804 |
| Net revenue from operations | 6,620 | 6,602 | 2,093 |
| Net revenue from discontinued operations (Note 8) | 3,480 | 3,573 | 5,276 |
| Excess of revenue over expenditure for the year | 10,100 | 10,175 | 7,369 |
| Retained earnings at beginning of year | - | - | - |
| | 10,100 | 10,175 | 7,369 |
| Contribution to the Province of Alberta | (10,100) | (10,175) | (7,369) |
| Retained earnings at end of year | $ - | $ - | $ - |

## THE ALBERTA GOVERNMENT TELEPHONES COMMISSION
## CONSOLIDATED STATEMENT OF CASH FLOWS
## FOR THE YEAR ENDED DECEMBER 31, 1998

(thousands of dollars)

| | 1998 | 1997 |
|---|---|---|
| Operating Activities: | | |
| Net revenue from operations | $ 6,602 | $ 2,093 |
| Changes in non-cash balances | 251 | 652 |
| | 6,853 | 2,745 |
| Discontinued operations (Note 8) | 7,592 | 4,278 |
| Cash provided by operating activities | 14,445 | 7,023 |
| Investing Activities: | | |
| Decrease in notes receivable | 200,000 | 400,000 |
| Discontinued operations (Note 8) | 1,894 | 10,996 |
| Cash provided by investing activities | 201,894 | 410,996 |
| Financing Activities: | | |
| Repayment of debenture debt | (200,000) | (400,000) |
| Increase in amount due to the Province of Alberta | 7,175 | 3,769 |
| Contribution to the Province of Alberta | (10,175) | (7,369) |
| | (203,000) | (403,600) |
| Discontinued operations (Note 8) | (2,766) | 447 |
| Cash applied to financing activities | (205,766) | (403,153) |
| Increase in cash and cash equivalents | 10,573 | 14,866 |
| Cash and cash equivalents at beginning of year | 92,460 | 77,594 |
| Cash and cash equivalents at end of year | $ 103,033 | $ 92,460 |

THE ALBERTA GOVERNMENT TELEPHONES COMMISSION
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 1998

Note 1 Authority

The Alberta Government Telephones Commission operates under the authority of the Telecommunications Act, Chapter T-3.5, Statutes of Alberta 1988, as amended and the Alberta Government Telephones Reorganization Act, Chapter A-23.5, Statutes of Alberta 1990.

Note 2 Summary of Significant Accounting Policies

(a) Basis of Consolidation

These consolidated financial statements include the accounts of the following wholly-owned subsidiaries:

— 475342 Alberta Ltd.,
NFI Finance, Inc.,
— NovAtel Finance, Inc.,
Systems Finance, Inc., and
— Cellular Finance Inc.

All subsidiaries are discontinued (see Note 8).

All significant transactions between these companies have been eliminated.

(b) Notes Receivable

Notes receivable are stated at cost, which includes principal amounts outstanding, less provisions for losses on loans. Interest on loans are recognized as income on the accrual basis unless the loans have been classified as non-performing.

(c) Valuation of Assets and Liabilities

Consistent with companies which are liquidating their operations, all assets and liabilities in liquidation are reflected at their estimated realizable value at the balance sheet date. Any gains or losses arising from revaluation of the assets and liabilities are included in the determination of excess of revenue over expense for the year.

(d) Income Taxes

The income tax provision is management's estimate of income taxes payable calculated on the basis that NFI Finance, Inc. and its subsidiaries had been wound up at December 31, 1998.

(e) Foreign Currency Translation

Commencing January 1, 1993, the foreign operations have been accounted for as self-sustaining operations. The assets and liabilities denominated in foreign currencies are translated into Canadian dollars at the exchange rates prevailing at the balance sheet date. Revenue and expenses are translated at average exchange rates prevailing during the year. Foreign currency translation adjustments are deferred and included in a separate component of equity described as "Foreign Currency Translation Adjustments."

All other monetary assets and liabilities denominated in foreign currencies are translated at the rate of exchange at the balance sheet date. Gains and losses are translated at the average exchange rate prevailing during the year. The resulting gains or losses are included in the determination of excess of revenue over expenses for the year.

Note 3 Cash and Cash Equivalents

| | 1998 | 1997 |
|---|---|---|
| | (thousands of dollars) | |
| Bank deposits | $ 894 | $ 353 |
| CCITF account | 63,407 | 58,560 |
| Short-term deposits | 38,732 | 33,547 |
| | $ 103,033 | $ 92,460 |

The Consolidated Cash Investment Trust Fund (CCITF) is a demand account managed by Alberta Treasury with the objective of providing competitive interest income to depositors while maintaining maximum security and liquidity of depositors' capital. The portfolio is composed of high quality short-term and mid-term fixed income securities with a maximum term to maturity of five years.

Short-term deposits are comprised of bank certificates that are reinvested as they mature.

Due to the short-term nature of cash and cash equivalents, the carrying value approximates fair value.

Note 4 Notes Receivable

| | 1998 | 1997 |
|---|---|---|
| | (thousands of dollars) | |
| Notes receivable | $ 6,000 | $ 208,000 |
| Sinking fund notes (Note 5) | 194,000 | 192,000 |
| | $ 200,000 | $ 400,000 |

The notes receivable were issued by TELUS Communications Inc., a subsidiary of TELUS Corporation, on October 4, 1990 pursuant to a debt reorganization agreement between the Commission, the Province of Alberta, and TELUS. The notes are comprised of residual and sinking fund notes issued in series that exactly match the Commission's debenture debt.

The notes bear interest at rates ranging from 11.8% to 12%. The rate for each series is 0.3% greater than that of the corresponding Commission debenture debt series, resulting in an interest premium of $909,000 (1997 - $1,533,000).

The notes matching those Commission debentures with sinking fund requirements are referred to as sinking fund notes.

The $150 million note that matures in 2003, has an early redemption provision at TELUS's option during the period 3 years to 6 months prior to maturity.

The fair value of the notes receivable is $218 million (1997 - $430 million). The Commission is required to hold the notes receivable until maturity date. The economic value to the Commission of the financial arrangement for the notes receivable and debentures is the interest premium.

The effective yield of the notes receivable equals the stated interest rate as the notes receivable are at par.

Note 5 Debenture Debt

Debentures are unconditionally guaranteed as to principal and interest by the Province of Alberta. The debenture deeds require annual sinking fund contributions of 1% of the principal amounts outstanding.

The $150 million debenture that matures in 2003, has an early redemption provisions at the Commission's option during the period 3 years to 6 months prior to maturity.

Anticipated requirements to meet debenture debt repayments and sinking fund provisions during the next five years are shown below. Sinking fund notes of TELUS Communications Inc. are held by the Commission to meet the sinking fund requirements.

Debenture maturity amounts are exactly offset by notes of TELUS Communications Inc. (Note 4).

Anticipated requirements to meet debenture debt repayments and sinking fund provision during the next five years are shown below. The following schedule assumes that the early redemption feature referred to in this note and Note 4 will not be exercised.

| | Debentures | Sinking Fund | Total |
|---|---|---|---|
| | | (thousands of dollars) | |
| 1999 | $ 50,000 | $ 1,500 | $ 51,500 |
| 2000 | - | 1,500 | 1,500 |
| 2001 | - | 1,500 | 1,500 |
| 2002 | - | 1,500 | 1,500 |
| 2003 | 150,000 | - | 150,000 |

The following table summarizes the maturities of the debenture debt:

| Date of Issue | Maturity Date | Interest Rate | Original Issue | Principal Outstanding |
|---|---|---|---|---|
| | | | (thousands of dollars) | |
| Nov 15, 1979 | Nov 15, 1999 * | 11.7 | $ 50,000 | $ 50,000 |
| May 31, 1983 | May 31, 2003 * | 11.5 | 150,000 | 150,000 |
| Total | | | | $ 200,000 |

* issues requiring sinking fund contributions

The fair value of the debentures is $216 million (1997 - $427 million). The economic value to the Commission of the financial arrangement for the debentures and notes receivable is the interest premium, as described in Note 4.

The effective yield of the debentures equals the stated interest rate as the debentures were issued at par.

Note 6 Due to the Province of Alberta

| | 1998 | 1997 |
|---|---|---|
| | (thousands of dollars) | |
| Balance at beginning of year | $ 57,921 | $ 54,152 |
| Net revenue (expenses) from discontinued operations: | | |
| NFI Finance, Inc. | 3,573 | 5,740 |
| 475342 Alberta Ltd. | - | (464) |
| | 3,573 | 5,276 |
| Net revenue from operations of the Commission | 6,602 | 2,093 |
| Payment made to the Province of Alberta | (3,000) | (3,600) |
| Balance at end of year | $ 65,096 | $ 57,921 |

Pursuant to section 15 of the Telecommunications Act, the amount due to the Province of Alberta can be paid, with the approval of the Lieutenant Governor in Council, with money that the Commission determines to be surplus.

Note 7 Foreign Currency Translation Adjustments

| | 1998 | 1997 |
|---|---|---|
| | (thousands of dollars) | |
| Balance at beginning of year | $ 977 | $ 781 |
| Translation adjustments for year arising from changes in foreign exchange rates | 87 | 196 |
| Balance at end of year | $ 1,064 | $ 977 |

Note 8 Discontinued Operations

Divestiture of NovAtel Communications Ltd.

In 1992, the Commission's wholly-owned subsidiary, NovAtel Communications Ltd. (NovAtel) underwent significant restructuring under which it:

- disposed of the cellular systems business and European operations to third parties, and
- disposed of the business of financing companies holding cellular system licences, the majority of land and buildings and certain other assets to subsidiary companies of the Commission.

The full amount of NovAtel's bank advances and long-term debt was assumed by the Province of Alberta through subsidiary companies of the Commission.

On May 29, 1992, the Commission disposed of 100% of the shares of NovAtel Communications Ltd. to a third party. Operating and divestiture losses incurred from January 1 to May 29, 1992 amounted to $116.6 million. Net liabilities assumed by the Province of Alberta through subsidiary companies of the Commission were $244.1 million at May 29, 1992.

Remaining subsidiaries of the Commission hold assets and liabilities retained from NovAtel after divestiture. The Commission is divesting itself of all assets of these subsidiaries.

| | 1998 | 1997 |
|---|---|---|
| | (thousands of dollars) | |
| Operating activities: | | |
| Net revenue from subsidiary companies | $ 3,573 | $ 5,276 |
| Provision for income taxes | 4,019 | 2,308 |
| Other non-cash items | - | (3,306) |
| Cash provided by operating activities | 7,592 | 4,278 |
| Investing activities: | | |
| Decrease in loans receivable | 424 | 10,996 |
| Disposal of property held for resale | 1,470 | - |
| Cash provided by investing activities | 1,894 | 10,996 |
| Financing activities: | | |
| (Decrease) increase in bank overdrafts | (2,766) | 447 |
| Cash applied to financing activities | (2,766) | 447 |
| Cash provided by discontinued operations | $ 6,720 | $ 15,721 |

Note 9 Contingencies

As a condition of the sale of NovAtel, the Commission through 475342 Alberta Ltd. (the Company) assumed the contingent liability related to a lawsuit against NovAtel that existed at May 29, 1992. An estimate of the potential recovery or loss to the Company cannot be made.

Note 10 Earn-out

On August 1, 1995 the Commission purchased from its subsidiary the right to receive, under certain conditions, amounts pursuant to the "earn-out" provisions of a 1992 agreement and a 1994 amending agreement. The "earn out" ($6,000,000) was payable in annual installments based on the payors' net income, due on April 1, 1996 to April 1, 1998. Any unpaid balance was payable on April 1, 1999. The balance of the amount due, $5,520,000, was paid in full in 1998 in advance of the due date. The Commission recognized the $5,520,000 as income when realized (1997 - $480,000).

Note 11 Fees and Benefits

The Commission and its subsidiaries did not pay any fees or benefits to their officers or directors in 1998 and 1997. The Commission and its subsidiaries have no employees.

Note 12 Budget

The 1998 budget was approved by management on August 4, 1998.

Note 13 Uncertainty Due to the Year 2000 Issue

The year 2000 issue arises because many computerized systems use two digits rather than four to identify a year. Date sensitive systems may recognize the year 2000 as 1900 or some other date, resulting in errors when information using the year 2000 is processed. In addition, similar problems may arise in some systems which use certain dates in 1999 to represent something other than the date. The effects of the year 2000 issue may be experienced before, on or after January 1, 2000, and, if not addressed, the impact on operations and financial reporting may range from minor errors to significant system failures. Even when management devotes time and effort to assess the effects of the year 2000 issue and implements a year 2000 plan, as is the case with the Commission, it is not possible to be sure that all aspects of the year 2000 issue affecting the entity, including those related to the efforts of customers, suppliers, and other third parties, will be fully resolved.

Note 14 Comparative Figures

The 1997 figures have been reclassified where necessary to conform to 1998 presentation.

ALBERTA TREASURY BRANCHES
CONSOLIDATED FINANCIAL STATEMENTS
MARCH 31, 1999



## AUDITOR'S REPORT

To the Provincial Treasurer

I have audited the consolidated balance sheet of Alberta Treasury Branches as at March 31, 1999, and the consolidated statements of income, changes in equity and cash flows for the year then ended. These consolidated financial statements are the responsibility of Alberta Treasury Branches' management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In my opinion, these consolidated financial statements present fairly, in all material respects, the financial position of Alberta Treasury Branches as at March 31, 1999 and the results of its operations and cash flows for the year then ended in accordance with generally accepted accounting principles.

Peter Valentine, FCA
Auditor General

Edmonton, Alberta
May 11, 1999

# ALBERTA TREASURY BRANCHES
# CONSOLIDATED BALANCE SHEET
## AS AT MARCH 31, 1999

(with comparative figures for 1998)

($ in thousands)

| | 1999 | 1998 |
|---|---|---|
| **ASSETS** | | |
| Cash resources (Note 2) | | |
| Cash and non-interest bearing deposits with Bank of Canada and other banks | $ 88,138 | $ 45,991 |
| Interest bearing deposits with Bank of Canada and other banks | 500,658 | 550,525 |
| Cheques and other items in transit, net | 6,296 | - |
| | 595,092 | 596,516 |
| Securities (Note 3) | 468,479 | 611,402 |
| Loans, net of allowance for credit losses (Notes 4 and 5) | | |
| Residential mortgages | 3,296,655 | 2,846,053 |
| Personal and credit card loans | 1,172,177 | 1,123,388 |
| Business and other loans | 3,567,943 | 3,490,983 |
| | 8,036,775 | 7,460,424 |
| Other | | |
| Capital assets (Note 6) | 54,171 | 50,843 |
| Other assets (Note 7) | 132,215 | 101,499 |
| | 186,386 | 152,342 |
| | $ 9,286,732 | $ 8,820,684 |
| **LIABILITIES AND EQUITY** | | |
| Deposits (Note 8) | | |
| Payable on demand | $ 1,568,233 | $ 1,555,967 |
| Payable after notice | 1,381,550 | 1,485,565 |
| Payable on a fixed date | 6,072,527 | 5,684,533 |
| | 9,022,310 | 8,726,065 |
| Other | | |
| Other liabilities (Notes 9 and 10) | 220,274 | 143,878 |
| Cheques and other items in transit, net | - | 17,285 |
| | 220,274 | 161,163 |
| Equity (deficit) | 44,148 | (66,544) |
| Commitments and contingent liabilities (Notes 13 and 20) | | |
| | $ 9,286,732 | $ 8,820,684 |

The accompanying notes are an integral part of the consolidated financial statements.

## ALBERTA TREASURY BRANCHES
## CONSOLIDATED STATEMENT OF INCOME
## FOR THE YEAR ENDED MARCH 31, 1999

(with comparative figures for 1998)

($ in thousands)

| | 1999 | 1998 |
|---|---|---|
| Interest income | | |
| Loans | $ 567,513 | $ 506,762 |
| Securities | 31,375 | 19,206 |
| Deposits with banks | 31,696 | 19,828 |
| | 630,584 | 545,796 |
| Interest expense | | |
| Deposits | 343,652 | 294,643 |
| Net interest income | 286,932 | 251,153 |
| Provision for credit losses (Note 5) | 3,787 | (4,173) |
| Net interest income after provision for credit losses | 283,145 | 255,326 |
| Non-interest income | | |
| Service charges | 35,733 | 32,313 |
| Credit fees | 16,200 | 14,515 |
| Commission and other | 11,280 | 8,439 |
| Card fees | 5,980 | 5,522 |
| Foreign exchange | 4,927 | 4,657 |
| | 74,120 | 65,446 |
| Net interest and other income | 357,265 | 320,772 |
| Non-interest expense | | |
| Salaries and employee benefits (Notes 10 and 11) | 119,950 | 120,083 |
| Premises and equipment, including amortization | 40,757 | 47,595 |
| Restructuring costs | 5,003 | 9,531 |
| Other | 80,863 | 58,129 |
| | 246,573 | 235,338 |
| Net income | $ 110,692 | $ 85,434 |

## ALBERTA TREASURY BRANCHES
## CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
## FOR THE YEAR ENDED MARCH 31, 1999

(with comparative figures for 1998)

($ in thousands)

| | 1999 | 1998 |
|---|---|---|
| Equity (deficit) at beginning of year | $ (66,544) | $ (151,978) |
| Net income for year | 110,692 | 85,434 |
| Equity (deficit) at end of year | $ 44,148 | $ (66,544) |

## ALBERTA TREASURY BRANCHES
## CONSOLIDATED STATEMENT OF CASH FLOWS
## FOR THE YEAR ENDED MARCH 31, 1999

(with comparative figures for 1998)

($ in thousands)

| | 1999 | 1998 |
|---|---|---|
| Cash flows from operating activities | | |
| Net income | $ 110,692 | $ 85,434 |
| Adjustments to determine net cash flows: | | |
| Provision for credit losses | 3,787 | (4,173) |
| Unrealized foreign exchange gain | (619) | (192) |
| Amortization | 11,674 | 17,148 |
| Net changes in accrued interest receivable and payable | 7,225 | 10,121 |
| Other items, net | (6,542) | (51,612) |
| | 126,217 | 56,726 |
| Cash flows from financing activities | | |
| Net change in deposits | 296,229 | 317,698 |
| Cash flows from investing activities | | |
| Net change in non-operating deposit balances with other banks | 49,842 | (69,208) |
| Purchase of investment securities | (4,540,665) | (4,869,258) |
| Maturity of investment securities | 4,683,588 | 4,725,018 |
| Net change in loans | (535,102) | (156,062) |
| Net purchases of capital assets | (15,002) | (9,453) |
| | (357,339) | (378,963) |
| Effect of exchange rate changes on cash and cash equivalents | 621 | 269 |
| Net change in cash and cash equivalents | 65,728 | (4,270) |
| Cash and cash equivalents at beginning of year | 28,706 | 32,976 |
| Cash and cash equivalents at end of year | $ 94,434 | $ 28,706 |
| Consists of: | | |
| Cash and non-interest bearing deposits with Bank of Canada and other banks | $ 88,138 | $ 45,991 |
| Cheques and other items in transit, net | 6,296 | (17,285) |
| | $ 94,434 | $ 28,706 |

## ALBERTA TREASURY BRANCHES
## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
## FOR THE YEAR ENDED MARCH 31, 1999
## ($ in thousands)

Alberta Treasury Branches (ATB) is an Agent of the Crown in right of Alberta and operates under the authority of the Alberta Treasury Branches Act, Statutes of Alberta, 1997, chapter A-37.9, proclaimed in force October 8, 1997. Under that Act, ATB was established as a provincial Crown corporation governed by a Board of Directors appointed by the Lieutenant Governor in Council. Prior to October 8, 1997, the Treasury Branches Deposits Fund operated under the authority of the Treasury Branches Act, Revised Statutes of Alberta 1980, chapter T7. Under Section 38 of the Alberta Treasury Branches Act, all property, assets, liabilities and obligations of the Treasury Branches Deposits Fund were transferred to ATB. ATB's primary business is providing financial services within Alberta.

Note 1 Significant accounting policies

The consolidated financial statements are prepared by management in accordance with generally accepted accounting principles. Comparative amounts have been reclassified where necessary to conform with the current year's presentation. The significant accounting policies followed in the preparation of these consolidated financial statements are summarized below:

(a) Basis of consolidation

The consolidated financial statements include the assets, liabilities and results of operations, after the elimination of intercompany transactions and balances of ATB and its wholly owned subsidiary, ATB Investment Services Inc., which commenced operations on October 31, 1997 for the purpose of distribution of mutual funds.

(b) Translation of foreign currencies

Foreign currency assets and liabilities are translated into Canadian dollars at rates prevailing at the date of the consolidated financial statements.

Foreign currency income and expenses are translated into Canadian dollars at the average rates throughout the year.

Realized and unrealized gains and losses on foreign currency transactions are included in other income in the Consolidated Statement of Income. Foreign exchange positions are hedged as much as is practical by forward exchange contracts.

(c) Use of estimates

In preparing the consolidated financial statements, management must make estimates and assumptions considering values of certain assets and liabilities, net income and related disclosures reported in these consolidated financial statements.

(d) Specific accounting policies

Other significant accounting policies are disclosed in the following notes with the related financial disclosure.

Note 2 Cash resources

Cash resources consist of cash, operating and investment deposits with banks and items in transit. Interest bearing deposits with banks are recorded at cost. Interest income on interest bearing deposits is recorded on an accrual basis. Cheques and other items in transit represent uncleared settlements with other banks and are recorded at cost.

If the total amount of uncleared settlements due to other banks exceeds the total amount of uncleared settlements owed to ATB, the net amount is reported under other liabilities on the Consolidated Balance Sheet.

Note 3 Securities

Securities are reported at cost or amortized cost, adjusted to recognize other than temporary losses in the underlying value. All securities held are investment account securities purchased with the intention to hold them to maturity, or until market conditions render alternative investments more attractive. Gains and losses on disposal of securities are included in income in the year of disposal. The cost or amortized cost of securities approximates the market value of securities.

All securities held mature within one year and the balances are as follows:

| | 1999 | 1998 |
|---|---|---|
| Issued or guaranteed by Canada | $ 48,212 | $ 82,085 |
| Other securities | 420,267 | 529,317 |
| | $ 468,479 | $ 611,402 |

In the ordinary course of business ATB pledges securities to the Bank of Canada in order to participate in clearing and payment systems and to have access to its facilities. Securities pledged at March 31, 1999 totalled $11,000, (1998 $13,000)

Note 4 Loans

Loans are stated net of any unearned interest and an allowance for credit losses. Interest income is recorded on an accrual basis, except for impaired loans, which are described below.

(a) Loan fees

Loan and commitment fees are recognized as other income over the term of the loan, or over the commitment period as appropriate.

(b) Impaired loans

Loans, except for credit cards, are classified as impaired when:

- There is no longer reasonable assurance as to the timely collection of the full amount of principal or interest.
- The principal or interest payments are 90 days past due.

Credit card loans are classified as impaired and fully provided for when principal or interest payments become 180 days past due.

When a loan is classified as impaired, interest income on the loan ceases to be accrued. No portion of cash received on an impaired loan is recorded as interest income until such time as any prior write-offs or specific allowances have been reversed.

Impaired loans are returned to performing status when there is reasonable assurance of the timely collection of all principal and interest, all arrears have been collected, and allowances for loan losses have been reversed.

Loans consist of the following:

| | 1999 | | | | 1998 |
|---|---|---|---|---|---|
| Type | Recorded Investment | Specific Allowances | General Allowance | Net Carrying Value | Net Carrying Value |
| Residential mortgages | $ 3,297,552 | $ 897 | $ - | $ 3,296,655 | $ 2,846,053 |
| Personal financing and credit card loans | 1,175,798 | 3,621 | - | 1,172,177 | 1,123,388 |
| Agricultural programs | 1,070,315 | 6,916 | - | 1,063,399 | 1,038,260 |
| Independent business, commercial, and other loans | 2,697,699 | 52,995 | - | 2,644,704 | 2,593,425 |
| General allowance | - | - | 140,160 | (140,160) | (140,702) |
| | $ 8,241,364 | $ 64,429 | $ 140,160 | $ 8,036,775 | $ 7,460,424 |

Impaired loans (included in the preceding schedule):

| | 1999 | | | | 1998 |
|---|---|---|---|---|---|
| Type | Recorded Investment | Specific Allowances | General Allowance | Net Carrying Value | Net Carrying Value |
| Residential mortgages | $ 13,175 | $ 897 | $ - | $ 12,278 | $ 14,571 |
| Personal financing and credit card loans | 6,587 | 3,621 | - | 2,966 | 3,930 |
| Agricultural programs | 40,624 | 6,916 | - | 33,708 | 22,105 |
| Independent business, commercial, and other loans | 119,122 | 52,995 | - | 66,127 | 271,838 |
| General allowance | - | - | 140,160 | (140,160) | (140,702) |
| | $ 179,508 | $ 64,429 | $ 140,160 | $ (25,081) | $ 171,742 |

The total recorded investment as at March 31, 1999, in assets acquired in satisfaction of problem loans was $2,971, with an allowance for losses of $207 and a net realizable value of $2,764 (1998: $70,568). These amounts are included in the preceding schedules.

Note 5 Allowance for credit losses

The allowance for credit losses is maintained at a level considered adequate to absorb credit related losses for all on and off-balance sheet items. Off-balance sheet items include loan guarantees, letters of credit, and derivative financial instruments.

The allowance for credit losses is deducted from the related asset category, except any amounts provided to cover potential losses from loan guarantees and letters of credit, which are included in other liabilities.

In establishing the net carrying value of the impaired loan portfolio, allowance has been made for potential legal actions by various borrowers. Management is of the view that it has strong defences and will vigorously defend such actions. However, previously established allowances will not be reversed until the outcome of such potential actions becomes clearer. Management is unable to estimate the amount of any such contingent gain.

(a) Specific allowances

Specific allowances on impaired loans are established on a loan-by-loan basis to reduce the carrying value of the impaired loans to the amount expected to be recovered. One of the following methods is used to determine the net realizable values:

- the discounted value of estimated future cash flows,
- the fair value of any underlying security discounted to the amount recoverable in the event of realization, or
- the observable market value for the loan.

Any change in the amount expected to be recovered on an impaired loan is charged or credited to the provision for credit losses.

(b) General allowance

This allowance recognizes that not all credit losses can be specifically identified on a loan-by-loan basis. The general allowance is computed based on the risk rating of performing loans. It is also based on management's judgement concerning the strength of the economy.

Changes in the allowance for credit losses are as follows:

| | 1999 | 1998 | 1999 | 1998 | 1999 | 1998 |
|---|---|---|---|---|---|---|
| | Specific Allowances | | General Allowance | | Total | |
| Balance at beginning of year | $101,843 | $205,123 | $140,702 | $ 46,068 | $242,545 | $251,191 |
| Provision for credit losses charged to the Consolidated Statement of Income | 4,329 | (98,807) | (542) | 94,634 | 3,787 | (4,173) |
| Write-offs | (22,100) | (50,257) | - | - | (22,100) | (50,257) |
| Recoveries | 25,357 | 45,784 | - | - | 25,357 | 45,784 |
| Balance at end of year | $109,429 | $101,843 | $140,160 | $140,702 | $249,589 | $242,545 |

Specific allowances as at March 31, 1999 of $109,429 represent an allowance for loan losses of $64,429 (Note 4) and an allowance for guarantee losses of $45,000 (Note 9).

## Note 6 Capital assets

Land is recorded at cost. Buildings, equipment and leasehold improvements are reported at cost less accumulated amortization. Amortization is calculated using the straight-line method over the estimated useful life of the related assets.

The maximum life limits for the various classes are as follows:

| | |
|---|---|
| Buildings | to 20 years |
| Leasehold improvements | to 10 years |
| Computer equipment and software | to 5 years |
| Other equipment | to 10 years |

Gains and losses on the disposal or write-down of capital assets are recorded in the Consolidated Statement of Income in the year of disposal.

As at March 31, 1999, the balances are as follows:

| | 1999 | | | 1998 |
|---|---|---|---|---|
| | Cost | Accumulated Amortization | Net Carrying Value | Net Carrying Value |
| Land | $ 7,338 | $ - | $ 7,338 | $ 7,356 |
| Buildings | 60,719 | 41,407 | 19,312 | 20,360 |
| Equipment and software | 76,008 | 59,357 | 16,651 | 14,173 |
| Leasehold improvements | 37,375 | 26,505 | 10,870 | 8,954 |
| | $ 181,440 | $ 127,269 | $ 54,171 | $ 50,843 |

Note 7 Other assets

Other assets are summarized as follows:

| | 1999 | 1998 |
|---|---|---|
| Accrued interest receivable | $ 106,684 | $ 91,429 |
| Other items, including accounts receivable, foreign exchange contracts and prepaid items | 25,531 | 10,070 |
| | $ 132,215 | $ 101,499 |

Note 8 Deposits

The repayment of all deposits, including accrued interest, is guaranteed by the Crown in right of Alberta.

The deposit guarantee was provided at no cost to ATB for the year ended March 31, 1998, and all prior years. Beginning April 1, 1998, a deposit guarantee fee, the base amount of which is equal to one-sixth of one percent of deposits held by ATB at the end of the year, will be assessed by the Crown. The fee is being introduced over a six-year period. For the year ended March 31, 1999, the fee equals 50% of the base amount, and will increase by 10% of the base amount each year until the year ending March 31, 2004.

On or before June 30, 1999, ATB will issue a non-convertible, non-redeemable, non-transferrable subordinated debenture privately placed with the Crown in right of Alberta in the amount of $7,519, maturing on June 30, 2004, bearing an interest rate of 5.475% payable semi-annually. This debenture is in full settlement of the deposit guarantee fee, which is recorded in other expenses on the Statement of Income for the year, and in other liabilities on the Balance Sheet as at March 31, 1999.

Deposits are summarized as follows:

| | Payable On Demand | Payable After Notice | Payable on a Fixed Date | 1999 Total | 1998 Total |
|---|---|---|---|---|---|
| Deposits by individuals | $ 489,947 | $ 1,108,273 | $ 3,628,098 | $ 5,226,318 | $ 4,972,460 |
| Deposits by businesses and governments | 1,078,286 | 273,277 | 2,444,429 | 3,795,992 | 3,753,605 |
| | $ 1,568,233 | $ 1,381,550 | $ 6,072,527 | $ 9,022,310 | $ 8,726,065 |

As at March 31, 1999, deposits by the Province of Alberta total $86,799 (1998: $134,441) and include deposits for loans made under the Alberta Farm Credit Stability Program in the amount of $86,220 (1998: $133,691).

Note 9 Other liabilities

Other liabilities are summarized as follows:

| | 1999 | 1998 |
|---|---|---|
| Accrued interest payable | $ 90,146 | $ 67,666 |
| Allowance for credit losses on off-balance sheet items | 45,000 | - |
| Other items, including accounts payable, deposit guarantee fee, foreign exchange contracts, pension liability and accrued liabilities | 85,128 | 76,212 |
| | $ 220,274 | $ 143,878 |

Note 10 Pension liability

ATB participates with other employers in the Public Service and Management Employees Pension Plans. These plans provide pensions for ATB's employees based on years of service and earnings.

Pension cost is disclosed as part of salaries, benefits and allowances. This includes the cost of pension benefits earned by employees during the year, interest on pension liabilities, and the amortization of deferred adjustments over the expected average remaining service life of the employee group.

ATB had an unfunded pension liability for each plan as at March 31, which was estimated as follows:

| | Public Service Pension Plan | Management Employees Pension Plan | 1999 | 1998 |
|---|---|---|---|---|
| Balance at beginning of the year | $ 2,666 | $ 9,012 | $ 11,678 | $ 18,683 |
| Decrease during the year | (630) | (2,755) | (3,385) | (7,005) |
| Balance at end of the year | $ 2,036 | $ 6,257 | $ 8,293 | $ 11,678 |

The total unfunded pension liability for each plan as at March 31, 1999 was determined by actuarial valuations as at December 31, 1997 extrapolated to March 31, 1999. The 1998 comparative figures were based on the actuarial valuations as at December 31, 1995 for the Public Service Pension Plan, and as at December 31, 1996 for the Management Employee Pension Plan, both extrapolated to March 31, 1998.

The actuarial valuations were determined using the projected benefit method prorated on service. Assumptions used in the valuation are based on the Pension Board's best estimate of future events. The plans' future experiences will inevitably vary, perhaps significantly, from the assumptions. Any differences between the actuarial assumptions and future experience will emerge as gains or losses in future valuations. Gains and losses which relate to the long term are amortized over the expected average remaining service life of the employee group. Gains and losses for which there is reasonable assurance regarding their measurement and realization are recognized in income immediately.

The Public Sector Pension Plans Act specifies the basis to determine the amount of the total unfunded liability for each plan which will be funded by employers. ATB's portion of those employers' liabilities was based on ATB's percentage of the total pensionable payroll of all employers in each plan.

The total liability is recorded in the Consolidated Balance Sheet under other liabilities. The change in the year is included in the Consolidated Statement of Income under salaries and employee benefits.

On April 29, 1999, Royal Assent was given to Bill 11, Public Sector Pension Plans Amendment Act. The amendments to the Act provide for the withdrawal of employers from the Management Employee Pension Plan (MEPP), the terms of which will be governed by regulation. ATB intends to withdraw from the MEPP and provide its own pension plan for management employees with benefits and entitlements that are no less favorable than the existing plan. The effective date of ATB's withdrawal from the MEPP will be established by regulation and it is intended that the withdrawal will be applied retroactively to December 31, 1998.

Following the withdrawal from the MEPP, ATB would have no continuing responsibility for the unfunded liability of the MEPP. As indicated above, as at March 31, 1999, ATB's share of the MEPP's unfunded liability amounted to $6,257. Based on a preliminary estimate by ATB's actuary, the value of the assets to be transferred from the MEPP will be sufficient to cover the liability of ATB's pension plan.

Note 11 Disclosure of salaries and benefits

ATB is an Agent of the Crown in right of Alberta, and as such, is required to disclose the following information as per the Salary and Benefits Disclosure Directive, made by the Treasury Board, pursuant to sections 5, 6 and 7 of the Financial Administration Act. This directive applies to all departments, regulated funds, provincial agencies and Crown-controlled organizations.

| | 1999 | | | 1998 |
|---|---|---|---|---|
| | Salary | Benefits and Allowances | Total | Total |
| Chairman of Board | $ 55 | $ - | $ 55 | $ 45 |
| Board Members (14) | 394 | - | 394 | 367 |
| President & CEO | 350 | 5 | 355 | 281 |
| Executive Vice-President, Branch Sales and Service (Position effective June 11, 1997) | 182 | 13 | 195 | 114 |
| Executive Vice-President, Marketing and Product Development (Position effective April 14, 1997) | 167 | 12 | 179 | 149 |
| Senior Vice-President, Credit | 128 | 13 | 141 | 113 |
| Senior Vice-President, Electronic and Centralized Services | 167 | 11 | 178 | 138 |

Salary includes all paid or approved regular base pay, overtime, bonuses, lump sum payments, honoraria, retroactive pay adjustments and any other direct cash remuneration.

Benefits and allowances consist of the employer's share of all employee benefits, and contributions or payments made on behalf of employees including pension, health care, dental coverage, vision coverage, medical benefits, group life insurance, accidental disability and dismemberment insurance, long-term disability plans, Employment Insurance, Canada Pension Plan, professional memberships and tuition. The benefits and allowances figure also includes the cost of additional benefits such as travel allowances, club membership allowances and car allowances.

An automobile was provided for the President & CEO; no amount is included in the benefits and allowances figure.

Note 12 Related party transactions

In the ordinary course of business, ATB provides normal banking services to various Province of Alberta departments and agencies on terms similar to those offered to non-related parties. (See Note 8)

Note 13 Commitments and contingent liabilities

(a) Credit instruments

In the normal course of business, ATB enters into various commitments to provide customers with sources of credit. These include credit commitments, letters of credit, letters of guarantee and loan guarantees.

Guarantees and standby letters of credit represent an irrevocable obligation to make payments to a third party in the event that the customer is unable to meet its financial or performance contractual obligations. In the event of a call on such commitments, ATB has recourse against the customers. Documentary and commercial letters of credit require ATB to honour drafts presented by third parties upon completion of specific activities. Guarantees include a loan guarantee relating to West Edmonton Mall as further disclosed in Note 20.

Commitments to extend credit represent undertakings to make credit available in the form of loans or other financing for specific amounts and maturities, subject to certain conditions, and include recently authorized credit not yet drawn down, and credit facilities available on a revolving basis.

These credit arrangements are subject to ATB's normal credit standards, and collateral may be obtained where appropriate. The contract amounts represent the maximum credit risk exposure to ATB should the contracts be fully drawn, and any collateral held proves to be of no value. As many of these arrangements will expire or terminate without being drawn upon, the contract amounts do not necessarily represent the future cash requirements.

| | 1999 | 1998 |
|---|---|---|
| Guarantees | $ 414,372 | $ 401,376 |
| Letters of credit | 9,974 | 10,437 |
| Commitments to extend credit | 1,511,451 | 1,405,109 |
| | $ 1,935,797 | $ 1,816,922 |

(b) Lease Commitments

ATB has obligations under long-term, non-cancellable operating leases for buildings and equipment. The future minimum lease payments for each of the next five years and thereafter are:

| | | |
|---|---|---|
| Year ending March 31, | 2000 | $ 16,134 |
| | 2001 | 13,204 |
| | 2002 | 11,518 |
| | 2003 | 9,686 |
| | 2004 | 8,322 |
| | 2005 and thereafter | 39,892 |
| | | $ 98,756 |

(c) Litigation

Various actions and legal proceedings arising from the normal course of business including the counterclaims described in Note 20 are pending against ATB. Management does not consider the aggregate liability, if any, of these actions and proceedings to be material.

## Note 14 Derivative financial instruments

ATB enters into derivative transactions in order to manage the risks associated with its interest rate exposure and other market risks. Derivative products used by ATB include interest rate swaps, interest rate caps, and index-linked swaps. The interest rate swaps and caps are used to manage exposures to fluctuations in interest rates in ATB's overall portfolio. The index-linked swaps, which are used to manage fluctuations in any underlying index, are entered into to hedge the risk arising from specific financial instruments. ATB only enters into these derivative instruments for its own account and does not act as an intermediary in this market.

The net income or expense related to derivative transactions is deferred and amortized over the term of the related agreement as an adjustment to interest income or interest expense in the Consolidated Statement of Income. The total amount of deferred expense at March 31, 1999 was $9,943 (1998: $4,869) and is recorded in Other Assets on the Consolidated Balance Sheet.

The derivative instruments are not included in the Consolidated Balance Sheet. The notional amount represents the amount to which a rate or price is applied in order to calculate the exchange of cash flows. The notional amounts are not exchanged and therefore are not at risk. Approved counterparties and maximum notional limits are established and monitored by management.

The notional amounts of derivative contracts are summarized as follows:

| | 1999 | | | 1998 |
|---|---|---|---|---|
| | Maturing Within 1 Year | Over 1 to 5 Years | Total | Total |
| Interest rate swaps | $ 175,000 | $ 400,000 | $ 575,000 | $ 175,000 |
| Index-linked swaps | 51,570 | 176,250 | 227,820 | 193,170 |
| Interest rate caps | - | 125,000 | 125,000 | 100,000 |
| | $ 226,570 | $ 701,250 | $ 927,820 | $ 468,170 |

The current replacement cost and fair value of derivative contracts is summarized as follows:

| | | | Current Replacement Cost | |
|---|---|---|---|---|
| | Notional Amount | Net Fair Value | Favourable Position | Unfavourable Position |
| Interest rate swaps | $ 575,000 | $ (897) | $ - | $ 897 |
| Index-linked swaps | 227,820 | 13,722 | 15,187 | 1,465 |
| Interest rate caps | 125,000 | (499) | - | 499 |
| | $ 927,820 | $ 12,326 | $ 15,187 | $ 2,861 |

Fair values are determined using pricing models which take into account current market and contractual prices of the underlying instruments, as well as time value and yield curve or volatility factors underlying the positions. Fair values have been segregated between those contracts which are in a favourable position (positive fair value) and those contracts which are in an unfavourable position (negative fair value).

Current credit exposure is limited to the amount of loss that ATB would suffer if every counterparty to which ATB was exposed were to default at once, which is represented by the current replacement cost of all outstanding contracts in a favourable position. ATB attempts to limit its credit exposure by dealing with counterparties believed to be credit-worthy.

## Note 15 Estimated fair value of balance sheet financial instruments

The amounts are designed to approximate the fair values of ATB's financial instruments using the valuation methods and assumptions described below. Since many of ATB's financial instruments lack an available trading market, the fair values represent estimates of the current market value of instruments, taking into account changes in market rates that have occurred since their origination. Due to the use of subjective assumptions and uncertainties, the fair value amounts should not be interpreted as being realizable in an immediate settlement of the instruments.

The carrying value of most of ATB's financial instruments is not adjusted to reflect changes in interest rates, as it is ATB's intention to hold the instruments to maturity.

The estimated fair values disclosed do not reflect the value of items that are not considered financial instruments, such as capital assets or intangible assets.

Estimated fair values of balance sheet financial instruments are summarized as follows:

| | 1999 | | | 1998 | | |
|---|---|---|---|---|---|---|
| | Carrying Value | Fair Value | Fair Value Over Carrying Value | Carrying Value | Fair Value | Fair Value Over Carrying Value |
| | $ | $ | $ | $ | $ | $ |
| Assets | | | | | | |
| Cash resources | 595,092 | 595,092 | - | 596,516 | 596,516 | - |
| Securities | 468,479 | 468,479 | - | 611,402 | 611,402 | - |
| Loans | 8,036,775 | 8,143,502 | 106,727 | 7,460,424 | 7,580,614 | 120,190 |
| Other assets | 132,215 | 132,215 | - | 101,499 | 101,499 | - |
| Liabilities | | | | | | |
| Deposits | 9,022,310 | 9,101,963 | 79,653 | 8,726,065 | 8,789,712 | 63,647 |
| Other | 220,274 | 220,274 | - | 161,163 | 161,163 | - |

Fair values were determined as follows:

Short-term financial instruments

For items which are short-term in nature, the estimated fair value is equal to carrying value. These include cash resources, securities, other assets and other liabilities.

Floating rate financial instruments

For floating rate financial instruments, fair value is equal to carrying value, as the interest rates automatically reprice to market.

Fixed rate financial instruments

For fixed rate loans, fair value is determined by discounting the expected future cash flows at market rates for loans with similar credit risks.

For fixed rate deposits, fair value is determined by discounting the contractual cash flows, using market interest rates currently offered for deposits with similar terms.

## Note 16 Interest rate risk

Interest rate risk is the risk that net interest income will decrease because of an adverse movement in interest rates. The following table details the gap between interest-sensitive assets and interest-sensitive liabilities, based on the earlier of the repricing or maturity date of both on and off-balance sheet assets and liabilities.

| 1999 | Within 3 Months | 3 - 6 Months | 6 - 12 Months | Total Within 1 Year | 1 Year to 5 Years | Over 5 Years | Non-Interest Sensitive | Total |
|---|---|---|---|---|---|---|---|---|
| Assets | | | | | | | | |
| Cash | $ 94,434 | $ | $ - | $ 94,434 | $ | $ | $ - | $ 94,434 |
| Effective interest rate | 5.07% | 0.00% | 0.00% | 5.07% | 0.00% | 0.00% | 0.00% | 5.07% |
| Investments | 803,601 | 37,849 | 127,687 | 969,137 | | | | 969,137 |
| Effective interest rate | 5.09% | 5.70% | 1.85% | 4.68% | 0.00% | 0.00% | 0.00% | 4.68% |
| Loans | 3,008,848 | 513,957 | 599,404 | 4,122,209 | 3,388,701 | 28,496 | 497,369 | 8,036,775 |
| Effective interest rate | 7.70% | 6.82% | 7.31% | 7.53% | 7.15% | 7.35% | 8.69% | 7.44% |
| Other | - | - | - | | - | - | 186,386 | 186,386 |
| | 3,906,883 | 551,806 | 727,091 | 5,185,780 | 3,388,701 | 28,496 | 683,755 | 9,286,732 |
| Liabilities and Equity | | | | | | | | |
| Deposits | 3,677,684 | 353,098 | 1,598,858 | 5,629,640 | 2,112,087 | - | 1,280,583 | 9,022,310 |
| Effective interest rate | 3.81% | 5.35% | 5.00% | 4.24% | 5.26% | 0.00% | 0.09% | 3.89% |
| Other | | | | - | - | | 264,422 | 264,422 |
| | 3,677,684 | 353,098 | 1,598,858 | 5,629,640 | 2,112,087 | - | 1,545,005 | 9,286,732 |
| On balance sheet gap | 229,199 | 198,708 | (871,767) | (443,860) | 1,276,614 | 28,496 | (861,250) | - |
| Derivatives used for asset/liability purposes (Notional amounts) | | | | | | | | |
| Pay side swaps | (150,000) | (25,000) | - | (175,000) | (400,000) | | | (575,000) |
| Effective interest rate | 5.01% | 6.07% | 0.00% | 5.16% | 5.62% | 0.00% | 0.00% | 0.00% |
| Receive side swaps | 425,000 | | 150,000 | 575,000 | - | - | - | 575,000 |
| Effective interest rate | 5.08% | 0.00% | 5.07% | 5.06% | 0.00% | 0.00% | 0.00% | 0.00% |
| Off-balance sheet gap | 275,000 | (25,000) | 150,000 | 400,000 | (400,000) | - | - | - |
| Net gap | $ 504,199 | $173,708 | $ (721,767) | $ (43,860) | $ 876,614 | $ 28,496 | $ (861,250) | $ - |
| % of assets | 5.43% | 1.87% | -7.77% | -0.47% | 9.44% | 0.31% | -9.27% | |

| 1998 | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Net gap | $ 347,607 | $277,240 | $ (550,641) | $ 74,206 | $ 543,680 | $ 279 | $ (618,165) | $ - |
| % of assets | 3.94% | 3.14% | -6.24% | 0.84% | 6.16% | 0.00% | -7.01% | |

The gap position is presented as of the close of the business day (March 31). It represents the position of ATB for that day only and may change significantly due to customer preferences and risk management policies.

Non-interest-bearing accounts are reported as non-interest sensitive. Due to the current rate environment, interest-bearing accounts which no longer demonstrate a direct correlation with market interest rate movements and are no longer deemed to be sensitive are reported as non-interest sensitive.

## Note 17 Credit risk

Credit risk is the risk of loss due to borrowers failing to meet their financial obligations. Credit risk arises from both on and off-balance sheet transactions. ATB's credit risk is significantly influenced by movements in the Alberta economy, which in recent years has shown strong growth and occasional sharp declines. The credit risk is managed to ensure diversification by limiting concentrations to single borrowers and high risk industries. The 1994 guarantee for the West Edmonton Mall financing disclosed in Note 20 is an exception. Further, policies and procedures are established to promote sound lending practices and ensure prompt attention to problem loans.

## Note 18 Market segment information

ATB conducts its business through market segments that offer different products and services – deposit business, individual lending, agricultural lending and independent business and commercial lending. The deposit business market segment provides a wide range of deposit and investment products and sundry financial services to all clients. The lending business market segments provide a variety of credit products and services designed specifically for each particular group of borrowers.

Results for these market segments are based on ATB's internal financial reporting systems and are consistent with the accounting policies followed in the preparation of ATB's consolidated statements. The assets and liabilities of the market segments are transfer-priced based on their nature and term to determine the net interest income. Non-interest expenses are currently not allocated to the business units.

| March 31, 1999 | Deposit Business | Lending Business: Individual | Lending Business: Agricultural | Lending Business: Independent Business and Commercial | Other *1 | Total |
|---|---|---|---|---|---|---|
| Net interest income | $ 125,847 | $ 63,477 | $ 25,286 | $ 62,711 | $ 9,611 | $ 286,932 |
| Other income | 29,801 | 6,183 | 1,577 | 8,595 | 27,964 | 74,120 |
| Total revenue | 155,648 | 69,660 | 26,863 | 71,306 | 37,575 | 361,052 |
| Provision for credit losses | | 660 | (680) | (40,651) | 44,458 | 3,787 |
| Non-interest expenses | | | | | 246,573 | 246,573 |
| Net income | $ 155,648 | $ 69,000 | $ 27,543 | $ 111,957 | $ (253,456) | $ 110,692 |
| Average loans | | 4,134,000 | 1,038,757 | 2,397,584 | 40,885 | 7,611,226 |
| Average deposits | 7,704,447 | | | | 1,185,610 | 8,890,057 |
| Total assets | | 4,468,832 | 1,063,399 | 2,644,704 | 1,109,797 | 9,286,732 |

| March 31, 1998 | Deposit Business | Lending Business: Individual | Lending Business: Agricultural | Lending Business: Independent Business and Commercial | Other *1 | Total |
|---|---|---|---|---|---|---|
| Net interest income | $ 103,750 | $ 62,199 | $ 24,019 | $ 64,342 | $ (3,157) | $ 251,153 |
| Other income | 27,398 | 4,921 | 1,592 | 8,217 | 23,318 | 65,446 |
| Total revenue | 131,148 | 67,120 | 25,611 | 72,559 | 20,161 | 316,599 |
| Provision for credit losses | | (3,493) | 5,691 | (101,005) | 94,634 | (4,173) |
| Non-interest expenses | | | | | 235,338 | 235,338 |
| Net income | $ 131,148 | $ 70,613 | $ 19,920 | $ 173,564 | $ (309,811) | $ 85,434 |
| Average loans | | 3,774,504 | 1,006,448 | 2,291,149 | 290,524 | 7,362,625 |
| Average deposits | 7,447,512 | | | | 1,112,244 | 8,559,756 |
| Total assets | | 3,969,441 | 1,038,260 | 2,593,425 | 1,219,558 | 8,820,684 |

*1 Comprised of business of a corporate nature such as investment, risk management, asset liability management, treasury operations and revenue and expenses not expressly attributed to the business units. It also includes the financial implications of the West Edmonton Mall guarantee, which is not typical of normal business activities of ATB. This issue is disclosed in Note 20.

## Note 19 Uncertainty due to the year 2000 issue

The year 2000 issue arises because many computerized systems use two digits rather than four to identify a year. Date-sensitive systems may recognize the year 2000 as 1900 or some other date, resulting in errors when information using the year 2000 date is processed. In addition, similar problems may arise in some systems which use certain dates in 1999 to represent something other than a date. The effects of the year 2000 issue may be experienced before, on, or after January 1, 2000, and, if not addressed, the impact on operations and financial reporting may range from minor errors to significant system failures, which could affect an entity's ability to conduct normal business operations. Even when management devotes substantial time and effort to assessing the effects of the year 2000 issue and implementing a year 2000 plan, as is the case with ATB, it is not possible to be certain that all aspects of the year 2000 issue affecting the entity, including those related to the efforts of customers, suppliers, and other third parties, will be fully resolved.

## Note 20 West Edmonton Mall loan guarantee

Under the terms of a guarantee agreement dated October 31, 1994, relating to the refinancing of West Edmonton Mall (WEM), ATB guaranteed to the Toronto Dominion Bank (TD Bank) repayment of a $353.3 million credit facility in accordance with the terms of the agreement, and in any event by October 31, 2004.

In the event that ATB is required to honour its guarantee, the net cost to ATB would be the difference between the amount then owed to the TD Bank and the proceeds from a realization or refinancing of WEM. During the year ATB obtained an appraisal that values WEM at $300.0 million. As a result of this appraisal, ATB has provided for a loan guarantee loss of $45.0 million, having regard to the difference between the appraised value and the amount owed to the TD Bank.

On August 25, 1998, ATB filed a Statement of Claim against the owners of WEM and others. ATB seeks to have the refinancing agreements set aside. ATB claims in the alternative that the owners of WEM have defaulted on their obligation to maintain the facility to the standard required under the loan agreements. ATB is applying to have the Court appoint an interim Receiver and Manager. It is management's opinion that if the failure to properly maintain the facility continues, the value of WEM could decline below the current $300.0 million, thereby, potentially increasing ATB's liability under its guarantee to the TD Bank. Any increase in ATB's liability under the guarantee would be charged against earnings in the year it is identified. However, management believes it has taken the necessary steps to minimize ATB's exposure under the guarantee to a point where a material addition to the existing provision is unlikely.

In April and June 1998, WEM provided ATB with copies of purported agreements dated November 15, 1994, February 23, 1996 and March 25, 1996, that purport to amend the WEM refinancing agreements dated October 31, 1994. The agreements purport to extend the term of the guarantee to 2014 and to amend the terms of repayment and other provisions of the refinancing agreements. Management believes that it will be successful in its legal action to set aside these purported amending agreements and as a result no liability to them has been established.

In December 1998, and January 1999, two counterclaims were filed in this action by the owners of West Edmonton Mall and others against ATB. These counterclaims are for significant amounts. In the opinion of management, these counterclaims are without merit and are unlikely to result in a material loss.

## ATB INVESTMENT SERVICES INC.
## FINANCIAL STATEMENTS
## MARCH 31, 1999



## AUDITOR'S REPORT

To the Board of Directors of ATB Investment Services Inc.

I have audited the balance sheet of ATB Investment Services Inc. as at March 31, 1999, and the statements of income, changes in shareholder's deficit and cash flows for the year then ended. These financial statements are the responsibility of ATB Investment Services Inc.'s management. My responsibility is to express an opinion on these consolidated financial statements based on my audit.

I conducted my audit in accordance with generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In my opinion, these financial statements present fairly, in all material respects, the financial position of ATB Investment Services Inc. as at March 31, 1999 and the results of its operations and cash flows for the year then ended in accordance with generally accepted accounting principles.

Peter Valentine, FCA
Auditor General

Edmonton, Alberta
May 11, 1999

## ATB INVESTMENT SERVICES INC.
## BALANCE SHEET
## AS AT MARCH 31

| | 1999 | 1998 |
|---|---|---|
| **ASSETS** | | |
| Current assets | | |
| Cash | $ 100,000 | $ 100,000 |
| Total assets | $ 100,000 | $ 100,000 |
| **LIABILITIES AND SHAREHOLDER'S DEFICIT** | | |
| Current liabilities | | |
| Interest payable | $ 9,171 | $ 2,476 |
| Other liabilities: | | |
| Due to ATB (Note 1) | 435,692 | 170,441 |
| Subordinated note (Note 2) | 99,000 | 99,000 |
| | 534,692 | 269,441 |
| Shareholder's deficit | | |
| Share capital (Note 3) | 1,000 | 1,000 |
| Deficit | (444,863) | (172,917) |
| | (443,863) | (171,917) |
| Total liabilities and shareholder's deficit | $ 100,000 | $ 100,000 |

The accompanying notes are an intergral part of these financial statements.

Craig Warnock
Director

Larry Kaumeyer
Director

## ATB INVESTMENT SERVICES INC.
## STATEMENT OF INCOME
## FOR THE YEAR ENDED MARCH 31

| | 1999 | *1998 |
|---|---|---|
| Commission income | $ 119,722 | $ 7,473 |
| Total income | $ 119,722 | $ 7,473 |
| Expenses | | |
| Administrative and selling expenses (Note 4): | | |
| Salaries & staff benefits | $ 101,710 | $ 21,118 |
| Professional | 173,350 | 101,535 |
| Other | 109,913 | 55,261 |
| | 384,973 | 177,914 |
| Interest expense | 6,695 | 2,476 |
| Total expenses | $ 391,668 | $ 180,390 |
| Net loss | $ 271,946 | $ 172,917 |

* Operations began October 31, 1997

## ATB INVESTMENT SERVICES INC.
## STATEMENT OF CHANGES IN SHAREHOLDER'S DEFICIT
## FOR THE YEAR ENDED MARCH 31

| | 1999 | 1998 |
|---|---|---|
| Share capital | $ 1,000 | $ 1,000 |
| Deficit | | |
| Deficit at beginning of year | (172,917) | - |
| Net loss for the year | (271,946) | (172,917) |
| Deficit at end of year | $ (444,863) | $ (172,917) |
| Total shareholder's deficit | $ (443,863) | $ (171,917) |

## ATB INVESTMENT SERVICES INC.
## STATEMENT OF CASH FLOWS
## FOR THE YEAR ENDED MARCH 31

| | 1999 | 1998 |
|---|---|---|
| Cash flows from operating activities | | |
| Net loss | $ (271,946) | $ (172,917) |
| Adjustments to determine net cash from operating activities: | | |
| Net change in current and other liabilities | 271,946 | 172,917 |
| Net change in cash | - | - |
| Cash at beginning of year | 100,000 | 100,000 |
| Cash at end of year | $ 100,000 | $ 100,000 |

## ATB INVESTMENT SERVICES INC.
## NOTES TO THE FINANCIAL STATEMENTS
## MARCH 31, 1999

ATB Investment Services Inc. (ATBIS) is a wholly owned subsidiary of Alberta Treasury Branches (ATB), an agent of the Crown in right of Alberta, established for the purpose of distributing mutual funds to customers of ATB. ATBIS was incorporated under the Business Corporations Act (Alberta) on October 3, 1997, by the Provincial Treasurer on behalf of the Treasury Branches Deposits Fund. The incorporation was approved by the Lieutenant Governor in Council under Alberta Order in Council 407/97, dated September 24, 1997. ATBIS began its operations on October 31, 1997.

Note 1 Due to ATB

In the normal course of operations, ATB pays expenses and collects revenues on behalf of ATBIS. These amounts are duly recorded on both ATB's and ATBIS's accounts. ATB management has agreed to defer the settlement of these amounts until such time when ATBIS generates adequate revenues to enable it to pay its obligations to ATB. The amounts due from (to) ATB at March 31 are as follows:

| | 1999 | 1998 |
|---|---|---|
| Due to ATB | $ 562,887 | $ 177,914 |
| Due from ATB | (127,195) | (7,473) |
| | $ 435,692 | $ 170,441 |

Note 2 Subordinated Note

The subordinated note held by ATB, is secured by a floating charge on all the assets of ATBIS, and bears interest at prime lending rate of ATB payable annually. The subordinated note has no specified maturity date, is repayable upon demand of ATB, and the redemption is subject to the prior approval of the Alberta Securities Commission. The principal balance as at March 31, 1999 was $99,000 (1998: $99,000).

Note 3 Share Capital

Authorized

An unlimited number of Class A voting common shares without nominal or par value.

An unlimited number of Class B non-voting common shares without nominal or par value.

An unlimited number of 10% non-cumulative redeemable non-voting preferred shares without nominal or par value.

Issued

| | |
|---|---|
| 100 Class A voting common shares for cash | $ 1,000 |

Note 4 Indirect Costs

In addition to direct costs, there are some indirect costs incurred by employees of ATB who performed administrative and selling services on behalf of ATBIS. Where readily determinable, these costs have been allocated and charged back to ATBIS. The amount charged for the year ending March 31, 1999, is $84,285 (1998: $7,480), and is included in administrative and selling expenses in the Statement of Income.

Note 5 Uncertainty Due to the year 2000 Issue

The year 2000 issue arises because many computerized systems use two digits rather than four to identify a year. Date-sensitive systems may recognize the year 2000 as 1900 or some other date, resulting in errors when information using the year 2000 date is processed. In addition, similar problems may arise in some systems which use certain dates in 1999 to represent something other than a date. The effects of the year 2000 issue may be experienced before, on, or after January 1, 2000, and, if not addressed, the impact on operations and financial reporting may range from minor errors to significant system failures, which could affect an entity's ability to conduct normal business operations. Even when management devotes substantial time and effort to assessing the effects of the year 2000 issue and implementing a year 2000 plan, as is the case with ATBIS, it is not possible to be certain that all aspects of the year 2000 issue affecting the entity, including those related to the efforts of customers, suppliers, and other third parties, will be fully resolved.

Note 6 Comparative Figures

The 1998 figures have been reclassified where necessary to conform to 1999 presentation.

CREDIT UNION DEPOSIT GUARANTEE CORPORATION
FINANCIAL STATEMENTS
DECEMBER 31, 1998



## AUDITOR'S REPORT

To the Directors of the
Credit Union Deposit Guarantee Corporation

I have audited the balance sheet of the Credit Union Deposit Guarantee Corporation as at December 31, 1998 and the statements of income and equity and cash flows for the year then ended. These financial statements are the responsibility of the Corporation's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In my opinion, these financial statements present fairly, in all material respects, the financial position of the Corporation as at December 31, 1998 and the results of its operations and its cash flows for the year then ended in accordance with generally accepted accounting principles.

Peter Valentine, FCA
Auditor General

Edmonton, Alberta
February 24, 1999

# CREDIT UNION DEPOSIT GUARANTEE CORPORATION
# BALANCE SHEET
# DECEMBER 31, 1998
(thousands of dollars)

| | 1998 | (restated) 1997 (Note 3) |
|---|---|---|
| **ASSETS** | | |
| Cash | $ 1,001 | $ 944 |
| Investments (Note 4) | 70,150 | 67,348 |
| Accrued interest receivable | 573 | 459 |
| Due from credit unions | 1,466 | 1,451 |
| Loans receivable | 278 | 483 |
| Other assets (Note 5) | 1,072 | 701 |
| Capital assets (Note 6) | 110 | 110 |
| | $ 74,650 | $ 71,496 |
| **LIABILITIES** | | |
| Accounts payable and accrued liabilities | $ 363 | $ 727 |
| Accrual for financial assistance (Note 7) | 5,515 | 5,865 |
| Deferred revenue | 895 | 928 |
| Amounts due to and investment in S C Financial Ltd. (Note 8) | 5,406 | 4,892 |
| | 12,179 | 12,412 |
| Commitments and Contingencies (Note 10) | | |
| **EQUITY** | | |
| Deposit Guarantee Fund (Note 3) | 60,167 | 56,782 |
| Master Bond Fund | 2,304 | 2,302 |
| | 62,471 | 59,084 |
| | $ 74,650 | $ 71,496 |

The accompanying notes and schedules are part of these financial statements.

# CREDIT UNION DEPOSIT GUARANTEE CORPORATION
## STATEMENTS OF INCOME AND EQUITY
## FOR THE YEAR ENDED DECEMBER 31, 1998

(thousands of dollars)

| | 1998 Budget | 1998 Actual | (restated) 1997 Actual (Note 3) |
|---|---|---|---|
| **Deposit Guarantee Fund** | | | |
| Revenue: | | | |
| Interest | $ 3,604 | $ 4,532 | $ 5,479 |
| Deposit guarantee assessments | 8,275 | 8,412 | 8,295 |
| Recovery of special assistance (Note 9) | 102 | 151 | 90 |
| | 11,981 | 13,095 | 13,864 |
| Expense: | | | |
| Interest and bank charges | 29 | 23 | 25 |
| Provision for (recovery of) financial assistance (Note 7) | 434 | 1,149 | (257) |
| Special contribution (Note 8) | 5,347 | 5,409 | 4,912 |
| Administration (Schedule 1) | 3,104 | 2,596 | 2,580 |
| | 8,914 | 9,177 | 7,260 |
| Income before income taxes | 3,067 | 3,918 | 6,604 |
| Income taxes (Note 11) | 310 | 533 | 796 |
| Net income for the year | 2,757 | 3,385 | 5,808 |
| Equity at beginning of year (Note 3) | 55,032 | 56,782 | 50,974 |
| Equity at end of year | $ 57,789 | $ 60,167 | $ 56,782 |
| **Master Bond Fund** | | | |
| Revenue: | | | |
| Assessments | $ 880 | $ 582 | $ 530 |
| Interest | 75 | 132 | 98 |
| | 955 | 714 | 628 |
| Expense: | | | |
| Insurance premium | 571 | 522 | 463 |
| Administration | 150 | 150 | 150 |
| Claims | 200 | 40 | (74) |
| | 921 | 712 | 539 |
| Net income for the year | 34 | 2 | 89 |
| Equity at beginning of year (Note 3) | 2,241 | 2,302 | 2,213 |
| Equity at end of year | $ 2,275 | $ 2,304 | $ 2,302 |

# CREDIT UNION DEPOSIT GUARANTEE CORPORATION
## STATEMENT OF CASH FLOWS
## FOR THE YEAR ENDED DECEMBER 31, 1998
(thousands of dollars)

| | 1998 Budget | 1998 Actual | 1997 Actual |
|---|---|---|---|
| Operating activities | | | |
| Assessments received | $ 8,982 | $ 8,946 | $ 8,785 |
| Interest received | 3,653 | 4,513 | 5,615 |
| Loan recoveries received | 40 | 242 | 120 |
| Special assistance received | 102 | 151 | 90 |
| Interest and bank charges paid | (29) | (23) | (25) |
| Claim recoveries (paid) | (200) | (40) | 74 |
| Income taxes paid | (821) | (1,252) | - |
| Financial assistance recoveries (paid) | (499) | (1,499) | 22 |
| Paid to suppliers and employees | (3,795) | (3,246) | (3,299) |
| Special contribution paid | (5,030) | (4,895) | (4,650) |
| Cash flows from operating activities | 2,403 | 2,897 | 6,732 |
| Investing activities | | | |
| Purchase of investments, net | (2,256) | (2,802) | (8,993) |
| Purchase of capital assets | (158) | (38) | (48) |
| Proceeds on disposal of capital assets | 11 | - | 16 |
| Cash flows from investing activities | (2,403) | (2,840) | (9,025) |
| Net increase (decrease) in cash | - | 57 | (2,293) |
| Cash at beginning of year | 650 | 944 | 3,237 |
| Cash at end of year | $ 650 | $ 1,001 | $ 944 |

# CREDIT UNION DEPOSIT GUARANTEE CORPORATION
## NOTES TO THE FINANCIAL STATEMENTS
## DECEMBER 31, 1998

Note 1 Authority and Purpose

The Credit Union Deposit Guarantee Corporation (the "Corporation"), operates under the authority of the Credit Union Act, Chapter C-31.1, Statutes of Alberta, 1989, as amended. The Corporation guarantees the repayment of all deposits with Alberta credit unions including accrued interest. The Credit Union Act provides that the Province of Alberta (Province) will ensure that this obligation of the Corporation is carried out. As at December 31, 1998 credit unions in Alberta held deposits totalling $4,771,124,000. Supervised credit unions receive assistance, support and direction in planning, policy and operational matters from the Corporation.

In 1986, S C Financial Ltd. was incorporated under the Alberta Business Corporations Act for the purpose of providing $335,000,000 of deficit financing assistance to credit unions under supervision. All of the outstanding shares of S C Financial Ltd. are held by the Corporation (Notes 2(c) and 8).

The Corporation guarantees the interest on the S C Financial Ltd. debentures issued in exchange for Stabilization Preferred Shares of the credit unions and the interest is funded by the Province pursuant to its indemnification. Accordingly, the obligation of the Corporation pursuant to its guarantee is not reported in these financial statements.

Note 2 Significant Accounting Policies and Reporting Practices

(a) Basis of Presentation

These financial statements have been prepared in accordance with generally accepted accounting principles.

These financial statements reflect separate funds: a Deposit Guarantee Fund and a Master Bond Fund.

The Deposit Guarantee Fund enables the Corporation to guarantee the repayment of all deposits with credit unions, its primary objective. The Deposit Guarantee Fund's statement of income includes assessments received from credit unions, assistance payments recorded on behalf of credit unions, as well as all other revenues and expenses related to the primary objective.

The Master Bond Fund provides insurance coverage to credit unions under a policy administered by the Corporation. A credit union may claim a maximum of $100,000 for directors liability claims and $85,000 for other claims, less its deductible, which is payable out of the Master Bond Fund; a reinsurance policy insures the amount of the claim that exceeds $100,000 or $85,000, respectively. The Master Bond Fund's statement of income includes insurance assessments received from credit unions, interest income, premiums paid for the reinsurance policy, administration fee, and claims.

The Corporation may use all of its assets to support its primary objective.

(b) Use of Estimates

The Corporation's financial statements are prepared in accordance with generally accepted accounting principles and necessarily include estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. The most significant areas requiring the use of estimates are the accrual for financial assistance and the provision for (recovery of) financial assistance, allowance for loan impairment and Master Bond Fund claims (expected and unreported). The Corporation reviews these estimates annually. Actual amounts could differ from those estimates depending upon certain future events and uncertainties.

(c) Non-consolidation of S C Financial Ltd.

The financial statements of the Corporation's wholly owned company, S C Financial Ltd., have not been consolidated with these financial statements since increases or decreases in the equity of S C Financial Ltd. do not accrue to the benefit of the Corporation.

(d) Cash

Cash consists of deposits in the Consolidated Cash Investment Trust Fund (CCITF) of the Province of Alberta. The CCITF is invested primarily in securities maturing in less than one year which are either issued or guaranteed by the Canadian federal and provincial governments, deposits given by or guaranteed by chartered banks, or short-term investment-grade-quality notes of Canadian corporations. Interest is earned on the daily cash balance at the average rate of earnings of the CCITF which varies depending on prevailing market interest rates.

(e) Investments

Investments are carried at cost or amortized cost, with any discount or premium amortized on a straight-line basis over the life of the investment. Investments are written down when there is a decline in value that is other than temporary. Gains and losses realized on disposal of investments are included in interest revenue.

(f) Loans Receivable

Impaired loans acquired as a result of credit unions or dissolution proceedings are recorded at estimated net realizable value. As future cash flows cannot be determined with reasonable reliability, estimated net realizable values are based on the fair value of security underlying the loans, net of expected costs of realization and disposal. Annually, management reviews the adequacy of the allowance for loan impairment on a loan by loan basis and adjusts the allowance to an amount considered adequate to provide for expected loan losses. No portion of cash received on an impaired loan is recorded as interest income until such time as any allowances have been reversed and the principal has been fully recovered.

(g) Capital Assets

The following rates are designed to amortize the cost of capital assets over their estimated useful lives:

| | |
|---|---|
| Furniture and equipment | five year straight-line |
| Computer equipment | 30 per cent declining-balance |
| Computer software | one year straight-line |
| Leasehold improvements | straight-line over lease term |

(h) Income Taxes

For the current year, the Corporation retroactively changed its method of recording income taxes from the tax allocation basis to the tax liability method. Therefore, future income taxes are recognized based on the tax effects that will arise if an asset is realized or a liability is settled for its carrying amount.

(i) Insurance Claims

The Corporation estimates and accrues the Master Bond Fund's share of losses from any reported claims. It makes an additional accrual of the estimated losses from unreported claims based on the last three years' average actual loss experience.

(j) Accrual for Financial Assistance

The Corporation recognizes financial assistance to specific credit unions as an expense when the need for assistance becomes likely and it can reasonably estimate the amount.

Additionally, an accrual for financial assistance is established by assessing the aggregate risk in the credit union system based on existing capital available in individual credit unions, current and anticipated market and economic conditions, the likelihood of losses, and the application of historic loss experience. It reflects management's best estimate of the losses arising from the inherent risk in the credit union system. Future economic conditions are not predictable with certainty and actual losses will vary from management's estimate.

(k) Fair Value of Financial Instruments

Most financial instruments are valued at their carrying amounts included on the balance sheet which are reasonable estimates of fair value. This approach applies to cash, accrued interest receivable, due from credit unions, loans receivable, accounts payable and accrued liabilities, accrual for financial assistance, amounts due to and investment in S C Financial Ltd. The fair values of investments are disclosed in Note 4.

Note 3 Prior Period Adjustments

The Corporation retroactively changed its method of recording income taxes to the tax liability method. As a result of this retroactive change, 1998 other assets has been increased by $117,000 (1997 $155,000) (Note 5) and income tax expenses have increased by $38,000 (1997 $427,000) (Note 11).

During the year, the Corporation also retroactively applied previously unused loss carry-forwards resulting from amending prior years' tax returns, to reduce the previous year's income tax provision by $227,000 and increase the 1998 equity by the same amount. As a result of this change, accounts payable has been reduced by $227,000 and income tax expense has been reduced by $227,000.

| | 1998 | 1997 |
|---|---|---|
| | (thousands of dollars) | |
| Deposit Guarantee Fund | | |
| Equity at beginning of year: | | |
| As previously reported | $ 56,400 | $ 50,392 |
| Prior period adjustment | 382 | 582 |
| As restated | $ 56,782 | $ 50,974 |

Note 4 Investments

| | Maturities | | | 1998 | | 1997 | |
|---|---|---|---|---|---|---|---|
| | Within 1 Year | Over 1 to 5 Years | Over 5 to 10 Years | Carrying Value | Market Value[2] | Carrying Value | Market Value |
| | (thousands of dollars) | | | | | | |
| Securities issued or guaranteed by: | | | | | | | |
| Canada | $ - | $16,425 | $23,974 | $40,399 | $41,287 | $42,020 | $42,545 |
| Provinces | - | 15,152 | 6,521 | 21,673 | 21,888 | 21,697 | 21,729 |
| Notes and term deposits issued by financial institutions: | 7,963 | - | - | 7,963 | 7,960 | 3,516 | 3,490 |
| | 7,963 | 31,577 | 30,495 | 70,035 | 71,135 | 67,233 | 67,764 |
| Shares of Credit Union Central Alberta Ltd. | - | - | 100 [1] | 100 | 100 | 100 | 100 |
| Shares of Co-operative Trust Company of Canada | - | - | 15 [1] | 15 | 15 | 15 | 15 |
| Total | $7,963 | $31,577 | $30,610 | $70,150 | $71,250 | $67,348 | $67,879 |
| Effective book yield | 4.85% | 5.35% | 5.32% | 5.28% | | 5.46% | |

[1] These securities have no specific maturity.

[2] Market values were calculated using independent pricing sources and Canadian investment dealers.

The market value of the investments is subject to fluctuation as a result of normal market risk. The principal factor influencing the market value is the prevailing rate of interest. An increase of 1 per cent in interest rates will result in a decrease of approximately $692,000 (1997 $652,000) in the market value of the total investments; and conversely, a decrease of 1 per cent in interest rates will result in an increase in the market value of the same amount.

## Note 5 Other Assets

| | 1998 | 1997 |
|---|---|---|
| | (thousands of dollars) | |
| Prepaid expenses | $ 567 | $ 546 |
| Income taxes recoverable | 388 | - |
| Future income taxes recoverable (Note 3) | 117 | 155 |
| | $ 1,072 | $ 701 |

## Note 6 Capital Assets

| | 1998 | 1997 |
|---|---|---|
| | (thousands of dollars) | |
| Furniture and equipment | $ 382 | $ 377 |
| Computer equipment | 262 | 269 |
| Computer software | 36 | 29 |
| Leasehold improvements | 63 | 63 |
| | 743 | 738 |
| Less: Accumulated amortization | (633) | (628) |
| Net book value | $ 110 | $ 110 |

## Note 7 Accrual for Financial Assistance

To fulfill the mandate described in Note 1, the Corporation assists credit unions experiencing financial difficulties when and as required. The Corporation monitors certain other credit unions experiencing financial difficulty and has a contingent responsibility to provide further financial assistance the amount of which, if any, is undeterminable at this time.

As part of an amalgamation arrangement, the Corporation committed in 1993 to provide financial assistance in an amount not to exceed $1,357,000. This amount was paid in full to the credit union during the year.

The book value of the accrual for financial assistance approximates its fair value as it represents the Corporation's best estimate of the future amounts to be paid.

| | 1998 | 1997 |
|---|---|---|
| | (thousands of dollars) | |
| Accrual for financial assistance: | | |
| Balance at beginning of year | $ 5,865 | $ 6,100 |
| Provision for (recovery of ) financial assistance | 1,075 | (235) |
| (Paid) during year | (1,425) | - |
| Balance at end of year | $ 5,515 | $ 5,865 |
| | | |
| Provision for (recovery of) financial assistance: | | |
| Financial assistance (recoveries), net of loan loss provisions (recoveries) | $ 74 | $ (22) |
| Provision for (recovery of) financial assistance | 1,075 | (235) |
| Provision for (recovery of) financial assistance | $ 1,149 | $ (257) |

Note 8 Amounts Due to and Investment in S C Financial Ltd.

| | 1998 | 1997 |
|---|---|---|
| | (thousands of dollars) | |
| Balance at beginning of year | $ 4,892 | $ 4,630 |
| Payment of previous year's special contribution | (4,892) | (4,630) |
| Special contribution current year | 5,409 | 4,912 |
| Special assistance due | (2) | (19) |
| | 5,407 | 4,893 |
| Shares | (1) | (1) |
| Balance at end of year | $ 5,406 | $ 4,892 |

The special contribution is an annual amount payable by the Corporation under the Credit Union Restructuring Agreement. It is equal to 0.11 per cent of credit union deposits and borrowings and is payable to S C Financial Ltd., as directed by the Province, until the year 2010.

Note 9 Recovery of Special Assistance

In 1989, the Corporation provided deficit assistance to supervised credit unions totalling $12,524,000. It may recover portions of this assistance based on a percentage of the credit unions' annual net income. The credit unions repaid $151,000 during the year (1997 - $90,000) and $2,581,000 to date.

Note 10 Commitments and Contingencies

(a) Lease commitments

The Corporation is committed to a non-cancellable operating lease for business premises totalling $345,000.

The following amounts represent minimum payments over the next three years:

| | |
|---|---|
| 1999 | $158,000 |
| 2000 | $160,000 |
| 2001 | $ 27,000 |

(b) Litigation

There are legal proceedings pending against the Corporation which arise from normal business activities. Management of the Corporation believes that the resolution of these proceedings will not be material to the financial position of the Corporation.

Note 11 Income Taxes

The Corporation is a deposit insurance corporation for income tax purposes. Its income excludes assessments and no deduction may be made for financial assistance paid on behalf of member credit unions. Income taxes are provided for at a rate of approximately 28% of earnings subject to tax.

At December 31, 1998 the Corporation had tax values of capital assets in excess of related book values of approximately $418,000 (1997 - $552,000), which are reflected in these financial statements as future income taxes (Note 5).

| | 1998 | 1997 |
|---|---|---|
| | (thousands of dollars) | |
| Current income taxes | $ 495 | $ 369 |
| Future income taxes (Note 3) | 38 | 427 |
| Income taxes | $ 533 | $ 796 |

## Note 12 Directors' and Management Remuneration

| | 1998 | | | 1997 |
|---|---|---|---|---|
| | Director Fees or Salary[1] | Benefits[2] and Allowances | Total | Total |
| | (thousands of dollars) | | | |
| Chair[4] | $ 33 | $ - | $ 33 | $ 40 |
| Board Members[4] | 48 | - | 48 | 36 |
| Chief Executive Officer | $ 135 | $ 21 | $ 156 | $ 141 |
| Senior management: | | | | |
| Chief Financial Officer | 89 | 16 | 105 | 101 |
| Senior Manager, Operations | 75 | 9 | 84 | 77 |
| Senior Manager, Credit[3] | 73 | 10 | 83 | 80 |
| Manager, Examinations | 65 | 8 | 73 | 66 |

(1) Salary includes regular base pay and bonuses.

(2) Employer's share of all employee benefits and contributions made on behalf of employees including Canada Pension Plan, Employment Insurance, group Registered Retirement Savings Plan, health care, dental coverage, vision coverage, medical benefits including out of country medical benefits, group life insurance, accidental disability and dismemberment insurance, long and short term disability, professional and club memberships, staff fund, automobile allowance and vacation payouts.

(3) The 1998 amounts represent one employee from January 1 to August 31 with $50,000 in salary and $8,000 in benefits, and another employee from September 1 to December 31 with $23,000 in salary and $2,000 in benefits.

(4) The Chair and Board Members are paid on a per diem basis for preparation and meeting time. The Deputy Provincial Treasurer is a Board Member but receives no remuneration from the Corporation.

## Note 13 1998 Budget

The 1998 budget was approved by the Board of Directors on September 30, 1997.

## Note 14 Comparative Figures

The 1997 figures have been restated where necessary to conform to 1998 presentation.

## Note 15 Uncertainty Due to Year 2000 Issue

The year 2000 issue arises because many computerized systems use two digits rather than four to identify a year. Date sensitive systems may recognize the year 2000 as 1900 or some other date, resulting in errors when information using the year 2000 is processed. In addition, similar problems may arise in some systems which use certain dates in 1999 to represent something other than the date. The effects of the year 2000 issue may be experienced before, on, or after January 1, 2000, and, if not addressed, the impact on operations and financial reporting may range from minor errors to significant system failures. Even when management devotes time and effort to assessing the effects of the year 2000 issue and implementing a year 2000 plan, as is the case with the Corporation, it is not possible to be sure that all aspects of the year 2000 issue affecting the Corporation, including those related to the efforts of customers, suppliers and other third parties, will be fully resolved in time.

## Note 16 Approval of Financial Statements

The Board of Directors has approved these financial statements.

# CREDIT UNION DEPOSIT GUARANTEE CORPORATION
## SCHEDULE OF ADMINISTRATION EXPENSES
## FOR THE YEAR ENDED DECEMBER 31, 1998
(thousands of dollars)

| | 1998 | | 1997 |
|---|---|---|---|
| | Budget | Actual | Actual |
| Deposit Guarantee Fund | | | |
| Salaries and benefits (Note 12) | $ 2,274 | $ 2,102 | $ 2,062 |
| Staff travel | 250 | 164 | 132 |
| Rental charges | 170 | 128 | 157 |
| Office | 123 | 97 | 115 |
| Board and committee fees (Note 12) | 122 | 81 | 76 |
| Professional fees | 110 | 70 | 76 |
| Other | 89 | 50 | 55 |
| Amortization | 82 | 38 | 43 |
| Board and committee expenses | 34 | 16 | 14 |
| | 3,254 | 2,746 | 2,730 |
| Allocation to Master Bond Fund | (150) | (150) | (150) |
| | $ 3,104 | $ 2,596 | $ 2,580 |

N.A. PROPERTIES (1994) LTD.
CONSOLIDATED FINANCIAL STATEMENTS
MARCH 31, 1999



## AUDITOR'S REPORT

To the Shareholder of N.A. Properties (1994) Ltd.

I have audited the consolidated balance sheet of N.A. Properties (1994) Ltd., as at March 31, 1999 and the consolidated statements of operations and deficit and cash flows for the year then ended. These financial statements are the responsibility of the Company's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In my opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at March 31, 1999, and the results of its operations and its cash flows for the year then ended in accordance with generally accepted accounting principles.

Peter Valentine, FCA
Auditor General

Edmonton, Alberta
May 10, 1999

N.A. PROPERTIES (1994) LTD.
CONSOLIDATED BALANCE SHEET
AS AT MARCH 31, 1999
(thousands of dollars)

| | 1999 | 1998 |
|---|---|---|
| **ASSETS** | | |
| Cash and cash equivalents | $ 3,719 | $ 951 |
| Accounts receivable | 13 | 117 |
| Mortgages and note receivable (Note 4) | 201 | 1,547 |
| Real estate property | 1 | 1 |
| Prepaid expenses | 2 | - |
| | 3,936 | 2,616 |
| Investment in Defeasance Fund (Note 5) | 115,550 | 104,970 |
| | $ 119,486 | $ 107,586 |
| **LIABILITIES** | | |
| Obligations under indemnities and commitments (Note 8) | $ 3,033 | $ 3,518 |
| Accounts payable | 307 | 329 |
| | 3,340 | 3,847 |
| Present value of future obligations (Note 5) | 115,550 | 104,970 |
| | 118,890 | 108,817 |
| **SHAREHOLDER'S EQUITY (DEFICIENCY)** | | |
| Share capital (Note 7) | 5,769 | 5,769 |
| Deficit | (5,173) | (7,000) |
| | 596 | (1,231) |
| | $ 119,486 | $ 107,586 |

On behalf of the Board:

Director – Robert Bhatia

Director – Peter McNeil

The accompanying notes are part of these consolidated financial statements.

## N.A. PROPERTIES (1994) LTD.
## CONSOLIDATED STATEMENT OF OPERATIONS AND DEFICIT
## FOR THE YEAR ENDED MARCH 31, 1999
(thousands of dollars)

| | 1999 Actual | 1998 Actual |
|---|---|---|
| Revenue | | |
| Real estate properties sold | $ - | $ 2,050 |
| Rental | 29 | 26 |
| Interest and other | 222 | 523 |
| | 251 | 2,599 |
| Expenses | | |
| Cost of real estate properties sold | - | 2,121 |
| Rental operating expense | 43 | 268 |
| General and administrative | 93 | 591 |
| Write down of note receivable | 12 | - |
| | 148 | 2,980 |
| Operating income (loss) before other items | 103 | (381) |
| Interest expense | - | 97 |
| Income (loss) before provision | 103 | (478) |
| (Recovery of) provision (Note 8) | (1,724) | 753 |
| Income (loss) for the year (Note 11) | 1,827 | (1,231) |
| Deficit, beginning of year | (7,000) | (11,008) |
| Receipt from Province of Alberta on indemnity (Note 2) | - | 5,239 |
| Deficit, end of year | $ (5,173) | $ (7,000) |

## N.A. PROPERTIES (1994) LTD.
## CONSOLIDATED STATEMENT OF CASH FLOWS
## FOR THE YEAR ENDED MARCH 31, 1999
(thousands of dollars)

| | 1999 | 1998 |
|---|---|---|
| Net inflow (outflow) of cash related to the following activities: | | |
| Operating | | |
| Gain (loss) for the year | $ 1,827 | $ (1,231) |
| Items not affecting cash: | | |
| (Recovery of) provision (Note 8) | (1,724) | 753 |
| Write down of note receivable | 12 | - |
| | 115 | (478) |
| Costs recovered from sale of real estate properties | - | 2,005 |
| Mortgages | | |
| Principal reductions | 1,935 | 413 |
| Mortgages sold | 615 | 2,335 |
| Net change in non-cash balances related to operations | 103 | (11) |
| | 2,768 | 4,264 |
| Financing | | |
| Bank indebtedness | - | (8,586) |
| Receipt from Province of Alberta on indemnity (Note 2) | - | 5,239 |
| | - | (3,347) |
| Net increase in cash during the year | 2,768 | 917 |
| Cash and cash equivalents beginning of year | 951 | 34 |
| Cash and cash equivalents end of year | $ 3,719 | $ 951 |

# N.A. PROPERTIES (1994) LTD.
## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
## MARCH 31, 1999

Note 1 Authority

The Company was continued on March 31, 1994 as an amalgamated corporation under the Business Corporation Act, Chapter B-15, Statutes of Alberta 1981, as amended. All issued shares of the Company are owned by the Province of Alberta and accordingly the Company is exempt from income tax.

Note 2 Nature of Operations

The Company's mandate is to dispose of all real estate properties, mortgages and accounts receivable held. The Company also has a long term obligation to administer the Defeasance Fund described in Note 5.

The Province of Alberta has indemnified the Company for all net losses, expenses or liabilities existing or subsequently incurred by the Company in its mandate of disposing of its assets.

There were no recoveries from the Province of Alberta in partial satisfaction of the indemnity in the year (1998 $5,239,000).

Note 3 Significant Accounting Policies

These consolidated financial statements have been prepared in accordance with generally accepted accounting principles, and within the framework of the accounting policies summarized below:

Basis of Consolidation

These consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, 356395 Alberta Ltd., and Terra Losa Centre Ltd. Separate audited financial statements have not been prepared for these subsidiaries as disclosure in these financial statements is adequate.

Mortgages

Mortgages are stated at cost, which includes amounts advanced, interest capitalized, accrued taxes and other charges, less repayments and an allowance for anticipated losses. Where a mortgage or loan bears interest at a rate below the prevailing market at the date of real estate property sale, a discount is recorded which is amortized into income over the term of the mortgage.

Real Estate Properties

The real estate property is stated at the lower of cost and estimated market value.

Investment in Defeasance Fund

Investments consist of bond coupons and residuals and are stated at cost with any discount or premium amortized on the basis of the underlying yield to maturity. Carrying values of investments are written down when there is a permanent impairment in value.

Revenue Recognition

Gains or losses on the sale of real estate properties are determined as the excess or deficiency of the proceeds of disposition over the carrying value of the disposed properties. Gains are recorded in income on disposal except in instances where a significant portion of the proceeds is not received in cash. In such circumstances, gains are deferred and recorded in income when significant cash proceeds are received.

Fair Value

The carrying value of cash, accounts receivable and accounts payable approximate their fair value due to the relatively short periods to maturity of the instruments. The fair value of other financial assets and liabilities are provided in the applicable notes to the financial statements.

Note 4 Mortgages and Note Receivable

Mortgages are secured by commercial property in Alberta. The one remaining mortgage earns interest at 7.5% and is the subject of renewal or pay out discussions. The stated value of mortgages is considered equivalent to fair value.

The non-interest bearing note receivable in the amount of $933,000 was issued in November 1987 and matures in the year 2027. The carrying value of the note receivable as at March 31, 1999 is $5,000. The note receivable is discounted by 20% based on the yield in effect at the time of issuance and adjusting the rate for a risk premium. The fair market value of the note at March 31, 1999 is estimated to be $16,000 using the current interest rate in effect and adjusting the rate for a risk premium.

Note 5 Investment in Defeasance Fund/Present Value of Future Obligations

The Fund consists of Government of Canada and provincial bond coupons and residuals which, together with the income earned thereon, is expected to accumulate to the sum not less than $335,000,000 on October 31, 2010. At that time, the Fund will be used to repay the principal of any outstanding debentures issued to credit unions under the terms of the Credit Union Deficit Financing Agreement dated October 31, 1986 and any excess will be paid to the Province. Credit Union Deposit Guarantee Corporation (CUDGC) will be responsible for any deficiency in the Fund.

As the income earned on these investments in the amount of $10,580,000 (1998 $9,561,000) does not accrue to the benefit of the Company, but rather to the benefit of the holders of the debentures and the Province, it is not included in income. Investments mature in the years 2009 and 2010 and the yield on the portfolio is approximately 9.77%. The fair value of the Defeasance Fund at March 31, 1999 is estimated to be $182,831,000.

Present Value of Future Obligations

Based on repayments of debentures by S C Financial Ltd. (SCF), a wholly-owned subsidiary of CUDGC, up to and including the Credit Unions' October 31, 1998 year end, the future obligations at October 31, 2010 would be $305,052,000 to the credit unions and the excess would be paid to the Province. These amounts will change based on future repayments of debentures through to October 31, 2010.

Interest on these debentures is at a rate per annum equal to the lesser of 14% and prime, and is payable by SCF.

Note 6 Indemnities and Commitments

The Company has provided indemnities of principal and interest on mortgages sold to a Canadian chartered bank. The principal and interest on these mortgages totalled $32,882,000 at March 31, 1999 (1998 $48,082,000). The Company's indemnities expire in part in 2001, 2002, 2003, 2016 and in full in 2017.

During the year the Company entered into transactions with a Canadian chartered bank whereby it sold mortgages at fair market value for a total consideration of $615,000 (1998 $2,335,000). For a period of one year after the sale the bank may require the Company to repurchase mortgages for any reason. After the first year, the bank must realize on the security underlying the mortgage prior to submitting a claim for a loss to the Company.

The Company entered into a contract to receive management services. Management and collection fees were paid in the amount of $70,000 (1998 $177,000).

The Company is obligated for monthly land lease payments and annual property taxes on the leased property, until the year 2018. The Company, in turn, leases the land to tenants.

## Note 7 Share Capital

Authorized

Unlimited number of Class "A" voting shares
Unlimited number of Class "B" voting shares
Unlimited number of Class "C" non-voting shares
Unlimited number of Class "D" non-voting shares
Unlimited number of Class "E" voting shares
Unlimited number of Class "F" non-voting shares

| | | 1999 | 1998 |
|---|---|---|---|
| | | (thousands of dollars) | |
| Issued | | | |
| 1 | Class "A" share | $ 5,768 | $ 5,768 |
| 1,000 | Class "B" shares | 1 | 1 |
| | | $ 5,769 | $ 5,769 |

## Note 8 (Recovery of) Provision

The provision for obligations under indemnities and commitments (Note 6) is based on an estimate of future costs to settle those obligations. Mortgage provisions have been determined based on an estimated value of security mortgage, repayment performance and foreclosures. Accounts receivable provision is based on the estimated recoverable value of the receivables.

The table below shows the change in the provision during the year.

| | 1999 | 1998 |
|---|---|---|
| | (thousands of dollars) | |
| Obligations for indemnities and commitments | $ (485) | $ 1,648 |
| Mortgage provisions - net of recoveries | (1,216) | (900) |
| Accounts receivable | (23) | 5 |
| | $ (1,724) | $ 753 |

## Note 9 Related Party Transactions

There were no related party transactions in the year ended March 31, 1999.

## Note 10 Fees and Salaries

There were no directors' fees or salaries paid during the year. The Company had no employees in 1999 and 1998.

## Note 11 Budget

The Company's 1998-99 annual budget appears in the Treasury's Business Plan in the Appendix to Budget 98. The budget projected a net expense for the year of $500,000. Since the company has liquidated most of its assets, a detailed budget was not prepared.

## Note 12 Uncertainty Due to the Year 2000 Issue

The year 2000 issue is the result of some computer systems using two digits rather than four to define the applicable year. Computer systems that have date sensitive software may recognize a date using "00" as the year 1900 rather than the year 2000, which could result in miscalculations or system failures. In addition, similar problems may arise in some systems if certain dates in 1999 are not recognized as a valid date or are recognized to represent something other than a date. The effects of the year 2000 issue may be experienced before, on, or after January 1, 2000. If not addressed, the effect on operations and financial reporting may range from minor errors to significant systems failure that could affect the ability to conduct some government operations. Despite management's efforts to address this issue, it is not possible to be certain that all aspects of the year 2000 issue affecting the Company, including those related to the efforts of customers, suppliers and other third parties, will be fully resolved.

S C FINANCIAL LTD.
FINANCIAL STATEMENTS
DECEMBER 31, 1998



## AUDITOR'S REPORT

The Shareholder of
S C Financial Ltd.

I have audited the balance sheet of S C Financial Ltd. as at December 31, 1998 and the statement of income for the year then ended. These financial statements are the responsibility of the Company's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In my opinion, these financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 1998 and the results of its operations and the changes in its cash flows for the year then ended in accordance with generally accepted accounting principles.

Peter Valentine, FCA
Auditor General

Edmonton, Alberta
February 19, 1999

# S C FINANCIAL LTD.
## BALANCE SHEET
## DECEMBER 31, 1998
(thousands of dollars)

| | 1998 | 1997 |
|---|---|---|
| **ASSETS** | | |
| Cash | $ 1 | $ 1 |
| Stabilization Preferred Shares (Note 3) | - | - |
| | $ 1 | $ 1 |
| **SHAREHOLDER'S EQUITY** | | |
| Share Capital | | |
| Authorized - Unlimited number of Class A shares | | |
| Issued - 10 Class A shares | $ 1 | $ 1 |
| | $ 1 | $ 1 |

The accompanying notes are part of these financial statements.

Approved on behalf of the Board:

J. Laitner, Director

R. A. Splane, Director

# S C FINANCIAL LTD.
## STATEMENT OF INCOME
## FOR THE YEAR ENDED DECEMBER 31, 1998
(thousands of dollars)

| | 1998 | | 1997 |
|---|---|---|---|
| | Budget | Actual | Actual |
| Revenue: | | | |
| Recovery on indemnity from the Province of Alberta (Note 3) | $ 11,663 | $ 14,727 | $ 10,294 |
| Special contribution from Credit Union Deposit Guarantee Corporation (Note 1 and 4) | 5,347 | 5,409 | 4,912 |
| | 17,010 | 20,136 | 15,206 |
| Expense: | | | |
| Interest on debentures (Note 3) | 17,010 | 20,136 | 15,206 |
| Net income for the year | $ - | $ - | $ - |

# S C FINANCIAL LTD.
## NOTES TO THE FINANCIAL STATEMENTS
## DECEMBER 31, 1998

Note 1 Authority and Purpose

S C Financial Ltd. (the Company) was incorporated on May 29, 1986 under the Alberta Business Corporations Act, as a wholly-owned entity of the Credit Union Deposit Guarantee Corporation (CUDGC), a Provincial Corporation. The Company is a deposit insurance corporation by virtue of it being a wholly-owned entity of a deposit insurance corporation. Accordingly, it is treated as such for income tax purposes.

Pursuant to the Credit Union Deficit Financing Agreement, the Company provided deficit financing assistance to supervised credit unions. In 1986, Stabilization Preferred Shares Series B were issued by credit unions to the Company in exchange for debentures totalling $335,000,000. CUDGC provided funds to the Company to purchase investments which will accumulate to $335,000,000 at October 31, 2010 in order to repay debentures outstanding and the balance to the Province of Alberta (Province) at that date (Note 3). Pursuant to an agreement, the Company transferred the investments to N.A. Properties (1994) Ltd. (wholly-owned by the Province). In exchange, N.A. Properties (1994) Ltd. assumed the Company's obligation totalling $335,000,000.

In 1989, CUDGC contributed $12,524,000 to the Company to provide cash deficit financing assistance to supervised credit unions in exchange for Stabilization Preferred Shares Series B.

The Credit Union Restructuring Agreement requires CUDGC to make an annual special contribution equal to 0.11% of credit union deposits and borrowings (loans payable) to the Company as directed by the Province, each year through to 2010. For the 1998 fiscal year, the special contribution was $5,409,000 (1997 $4,912,000).

Note 2 Financial Statement Presentation

A cash flow statement is not provided as disclosure in these financial statements is considered to be adequate. Operating or administrative costs of the Company are paid by CUDGC.

Note 3 Stabilization Preferred Shares

The Stabilization Preferred Shares Series B have no value to the Company itself because any redemptions thereon flow through the Company and accrue to the benefit of the Province or CUDGC. Therefore, these shares do not appear as an asset with value on the balance sheet of the Company.

The Stabilization Preferred Shares are non-voting and are not entitled to dividends. They are redeemable at the option of the credit unions for the issue price, or otherwise shall be redeemed in an amount equal to 25% through 1999 inclusive, and 50% thereafter, of the annual net income of the credit unions. Any funds received in respect of redemption of the Stabilization Preferred Shares are used on a pro rata basis to repay the debentures and CUDGC. The amount of debentures outstanding after the 1998 redemptions is $305,052,000. The future obligation of N.A. Properties (1994) Ltd. (see Note 1) would be $305,052,000 to the credit unions and $29,948,000 to the Province at October 31, 2010. These amounts will change based on annual redemptions through to October 31, 2010. The present value of this future obligation is $112,824,000 which is supported by assets with an amortized cost of $112,824,000 held by N.A. Properties (1994) Ltd.

On a quarterly basis, the Company pays interest on the debentures at the lesser of 14% or prime. CUDGC, with an indemnity from the Province, guarantees payment of the interest.

Note 4 Due to Related Parties

Transactions with related parties are undertaken to meet funding commitments under the Credit Union Deficit Financing Agreement and Credit Union Restructuring Agreement. Balances have been disclosed on a net basis in these financial statements to reflect the flow-through nature of the transactions.

| | 1998 | 1997 |
|---|---|---|
| | (thousands of dollars) | |
| Redemption of Stabilization Preferred Shares: | | |
| Due from credit unions | $ 55 | $ 549 |
| Due to credit unions on repayment of debentures | (53) | (530) |
| Due to Credit Union Deposit Guarantee Corporation | (2) | (19) |
| | - | - |
| Interest on debentures: | | |
| Due to credit unions | (3,535) | (2,809) |
| Due to Province to fund interest | (1,874) | (2,103) |
| Due from Credit Union Deposit Guarantee Corporation - special contribution | 5,409 | 4,912 |
| | - | - |
| | $ - | $ - |

Note 5 1998 Budget

The 1998 budget was approved by the Board of Directors on September 30, 1997.

Note 6 Comparative Figures

The 1997 figures have been restated where necessary to conform to 1998 presentation.

Note 7 Uncertainty due to the Year 2000 Issue

The year 2000 issue arises because many computerized systems use two digits rather than four to identify a year. Date sensitive systems may recognize the year 2000 as 1900 or some other date, resulting in errors when information using the year 2000 is processed. In addition, similar problems may arise in some systems which use certain dates in 1999 to represent something other than the date. The effects of the year 2000 issue may be experienced before, on, or after January 1, 2000, and, if not addressed, the impact on operations and financial reporting may range from minor errors to significant system failures. Even when management devotes time and effort to assessing the effects of the year 2000 issue and implementing a year 2000 plan, as is the case with the Company, it is not possible to be sure that all aspects of the year 2000 issue affecting the Company, including those related to the efforts of customers, suppliers and other third parties, will be fully resolved in time.

CHEMBIOMED LTD.
FINANCIAL STATEMENTS
MARCH 17, 1999



## AUDITOR'S REPORT

To the Shareholders of Chembiomed Ltd.

I have audited the balance sheet of Chembiomed Ltd., as at March 17, 1999 and the statement of liquidation activities and deficit and the statement of cash flows for the period April 1, 1998 to March 17, 1999. These financial statements are the responsibility of the Company's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In my opinion, these financial statements present fairly, in all material respects, the financial position of the Company as at March 17, 1999 and the results of its liquidation activities and its cash flows for the period April 1, 1998 to March 17, 1999 then ended in accordance with the disclosed basis of accounting as described in Note 2 to the financial statements.

Peter Valentine, FCA
Auditor General

Edmonton, Alberta
April 22, 1999

## CHEMBIOMED LTD.
## BALANCE SHEET
## MARCH 17, 1999
(comparative figures as at March 31, 1998)

| | 1999 | 1998 |
|---|---|---|
| **ASSETS** | | |
| Current assets: | | |
| Cash | $ - | $ 334,942 |
| Accounts receivable | - | 14,441 |
| | - | 349,383 |
| Patents (Note 4) | - | 1 |
| | $ - | $ 349,384 |
| **LIABILITIES AND SHAREHOLDERS' DEFICIENCY** | | |
| Current liabilities: | | |
| Accounts payable and accrued liabilities | $ - | $ 40,770 |
| Due to a shareholder (Note 5) | - | 308,614 |
| | - | 349,384 |
| Shareholders' deficiency | | |
| Share capital (Note 6) | - | 40,928,430 |
| Deficit | - | (40,928,430) |
| | - | - |
| | $ - | $ 349,384 |

Approved by the Board

Director – Robert Bhatia

Director – Peter McNeil

The accompanying notes are part of these financial statements.

## CHEMBIOMED LTD.
## STATEMENT OF LIQUIDATION ACTIVITIES AND DEFICIT
## FOR THE PERIOD FROM APRIL 1, 1998 TO MARCH 17, 1999
(with comparative figures for the year ended March 31, 1998)

| | 1999 | 1998 |
|---|---|---|
| Revenue: | | |
| Gain on revaluation of assets and liabilities (Note 7) | $ 329,968 | $ 20,935,811 |
| Interest income | 14,869 | 9,194 |
| Recoveries | 4,454 | 6,596 |
| Sales | - | 11,142 |
| Other | - | 16,408 |
| | 349,291 | 20,979,151 |
| Expense: | | |
| Operating | 148 | 45,859 |
| Excess of revenue over expense for the period/year | 349,143 | 20,933,292 |
| Deficit at beginning of year | (40,928,430) | - |
| Reduction of share capital (Note 6) | 40,579,287 | (61,861,722) |
| Deficit at end of period/year | $ - | $(40,928,430) |

# CHEMBIOMED LTD.
## STATEMENT OF CASH FLOWS
## FOR THE PERIOD FROM APRIL 1, 1998 TO MARCH 17, 1999
(with comparative figures for the year ended March 31, 1998)

| | 1999 | 1998 |
|---|---|---|
| Operating activities: | | |
| Income for the period/year | $ 349,143 | $ 20,933,292 |
| Decrease (increase) in accounts receivable | 14,441 | (1,303) |
| Decrease in current liabilities | (349,384) | (20,895,510) |
| Decrease in assets | 1 | - |
| Increase in cash | 14,201 | 36,479 |
| Cash at beginning of period/year | 334,942 | 298,463 |
| Cash transferred to the province | (349,143) | - |
| Cash at end of period/year | $ - | $ 334,942 |

# CHEMBIOMED LTD.
## NOTES TO THE FINANCIAL STATEMENTS
## MARCH 17, 1999

Note 1 Discontinuance of Operations

Chembiomed Ltd. was a Company incorporated under the Canada Business Corporations Act. The Company's share capital was owned by the Province of Alberta and The University of Alberta (U of A).

The Company transferred its assets comprising technology and chemical inventory to Alberta Research Council (ARC) effective March 15, 1999 to facilitate a Collaborative Research Agreement between the ARC and the U of A using the technology which was developed by the Company.

Industry Canada issued a Certificate of Dissolution of Chembiomed dated March 17, 1999. The Company did not receive confirmation of the dissolution until April 13, 1999. Upon the Company receiving confirmation, the remaining cash in the amount of $349,143 was paid to the Province in accordance with the Special Resolution of Shareholders (Note 6).

Note 2 Significant Accounting Policies

Basis of accounting

All assets and liabilities are reflected at their estimated realizable value. Any gains or losses from re-evaluation of the assets and liabilities are recognized in the net gain for the year.

Inventories

Chemical inventories at March 17, 1999 and March 31, 1998 were recorded as having no value.

Note 3 Income Taxes

The Company is a provincial corporation, therefore was exempted from paying taxes.

Note 4 Patents

The Company held a number of international patents.

Under the provisions of a technology transfer agreement, the ARC could use or sub-licence the Company's patents, intellectual property, proprietary information, bioactive carbohydrate research program and all other technology. The ARC was not permitted to use any of the transferred items directly in commercial production, but could do so by way of sub-licences. Under such sub-licencing arrangements, the Company was entitled to receive royalties, after deducting certain costs of the ARC, equal to the proportionate contribution to the commercial production of the value of the items transferred.

On April 28, 1995 an agreement was signed with ARC which transferred the right to grant sub-licences for the Company's chemical inventory. An exclusive sub-licence agreement was signed with a private sector research company for the use and sale of certain of the Company's chemical inventory for which the Company was entitled to receive royalty revenue. Royalty revenue was not determinable until some time in the future when the private sector research company sold to an unrelated party.

ARC had the right, but not the obligation, to maintain and protect any of the transferred patents. The Company could also maintain and protect any such patents that the ARC abandoned.

As the realizable value of the patents could not be reasonably ascertained, they were written down to a nominal carrying value of $1. On March 15, 1999 all rights to patents were transferred to Alberta Research Council in order to facilitate a Collaborative Research Agreement between Alberta Research Council and the University of Alberta using technology which originated in Chembiomed.

Note 5 Due to a Shareholder

During 1992, the Province of Alberta provided funding for the Company in the amount of $7,000,000 which was secured by promissory notes. The notes bear interest at bank prime rate, calculated and payable semi-annually. Payment on the notes was demanded on September 30, 1994.

In October 1994, the Province of Alberta provided funding to the Company in the amount of $13,224,759 to pay down the long-term debt and accrued interest. The amount due was subsequently reduced by the proceeds from the sale of the land and building of $3,650,000 and a payment of $700,000. The remaining amount due of $8,874,759 bearing interest at 9.89% per year was further reduced to $308,614, the amount estimated to be realizable by the Province of Alberta. Payment on the amount due was demanded on November 8, 1994.

On July 28, 1998, the Province of Alberta forgave the indebtedness of Chembiomed. The resolution of this indebtedness was necessary to facilitate the voluntary wind up of the Company and the Collaborative Research Agreement described in Note 1.

Note 6 Share Capital

Authorized
4,275,000 non-participating non-voting preferred shares with a stated value of $10 per share,
Unlimited number of common shares

| | 1999 | 1998 |
|---|---|---|
| Issued and outstanding prior to dissolution | | |
| 3,065,909 preferred shares | $ 30,577,586 | $ 30,577,586 |
| 1,126,924 common shares | 10,350,844 | 10,350,844 |
| Reduction of share capital | (40,579,287) | - |
| Cancelled and distributed to shareholder upon dissolution of Company | (349,143) | - |
| | $ - | $ 40,928,430 |

On March 12, 1999, the shareholders approved the voluntary dissolution of the Company, pursuant to the provisions of the Business Corporations Act (Canada). The stated capital of the Company's shares in the amount of $40,928,430 was reduced by the deficit of $40,579,287 and the balance of $349,143 in cash was distributed to the Province of Alberta (see Note 1).

Note 7 Gain on revaluation of assets and liabilities

| | 1999 | 1998 |
|---|---|---|
| Reduction of amount due to Province | $ 308,614 | $ 20,935,811 |
| Reversal of liquidation expense | 21,355 | - |
| Revaluation of assets | (1) | - |
| | $ 329,968 | $ 20,935,811 |

Note 8 Related Party Transactions

The cash assets of the Company were transferred to the Province. The remaining assets were transferred to ARC for $1 (see Note 1).

Note 9 Budget and Salary Disclosure

No budget was approved as the Company is in liquidation. Also there is no salary disclosure as the Company had no paid directors or employees.

## GAINERS INC.
## CONSOLIDATED FINANCIAL STATEMENTS
## SEPTEMBER 30, 1998



## AUDITORS' REPORT

To the Shareholder of Gainers Inc.

We have audited the consolidated balance sheet of Gainers Inc. as at September 30, 1998 and the consolidated statements of operations and deficit, and changes in financial position for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Company as at September 30, 1998 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles.

PricewaterhouseCoopers LLP
Chartered Accountants

Edmonton, Alberta
November 13, 1998

## GAINERS INC.
## CONSOLIDATED BALANCE SHEET
(in thousands of dollars)

| | September 30 1998 | September 27 1997 |
|---|---|---|
| **ASSETS** | | |
| Cash | $ 19 | $ 14 |
| Accounts receivable | 1,298 | 809 |
| Prepaid expenses | 15 | |
| Fixed assets | 77 | 59 |
| Other assets (Note 3) | - | 240 |
| | $ 1,409 | $ 1,122 |
| **LIABILITIES** | | |
| Accounts payable and accrued liabilities | $ 1,421 | $ 358 |
| Principal and interest on prior years' income taxes (Note 4) | 6,471 | 6,036 |
| Long-term debt (Note 5) | 201,513 | 199,978 |
| | 209,405 | 206,372 |
| **CAPITAL AND DEFICIT** | | |
| Share capital (Note 6) | 1 | 1 |
| Contributed surplus | 15,002 | 15,002 |
| Deficit | (222,999) | (220,253) |
| | (207,996) | (205,250) |
| | $ 1,409 | $ 1,122 |

Contingencies (Note 7)

Approved by the Board D. Harrington, Director

## GAINERS INC.
## CONSOLIDATED STATEMENT OF OPERATIONS AND DEFICIT
(in thousands of dollars)

| | Year ended September 30 1998 | Year ended September 27 1997 |
|---|---|---|
| Income | | |
| Lease revenue and other income | $ 238 | $ 366 |
| Expenses | | |
| General and administrative | 2,534 | 1,122 |
| Other costs | | |
| Interest on income tax reassessment | 450 | 436 |
| | 2,984 | 1,558 |
| Loss for the year | (2,746) | (1,192) |
| Deficit at beginning of year | (220,253) | (219,061) |
| Deficit at end of year | $(222,999) | $(220,253) |

## GAINERS INC.
## CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION
(in thousands of dollars)

| | Year ended September 30 1998 | Year ended September 27 1997 |
|---|---|---|
| Cash was provided by (used for) | | |
| Operations | | |
| Loss for the year | $ (2,746) | $ (1,192) |
| Net change in non-cash balances | 1,234 | 1,223 |
| Total from operations | (1,512) | 31 |
| Financing activities | | |
| Repayment of long-term debt | (373) | (17) |
| Proceeds from long-term debt | 1,908 | - |
| Total from financing | 1,535 | (17) |
| Investment activity | | |
| Proceeds on disposal of assets | (18) | - |
| Increase (decrease) in cash for the year | 5 | 14 |
| Cash at beginning of year | 14 | - |
| Cash at end of year | $ 19 | $ 14 |

## GAINERS INC.
## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
## SEPTEMBER 30, 1998
(tabular amounts in thousands of dollars)

Note 1 Basis of presentation

The consolidated financial statements of the Company include the accounts of Gainers Inc. and its wholly-owned subsidiary companies: Gainers Properties Inc. ("GPI") and MPF Note Inc. (collectively the "Company"). MPF Note Inc. was inactive during the year.

Through September 25, 1993, the Company operated on a going-concern basis, which contemplated the realization of assets and discharge of liabilities in the normal course of business. Events since that date have resulted in the discontinuance of all ongoing business.

Note 2 Investment in and amounts due from former affiliates

The investment is comprised of 77,500 Class A preferred shares of Pocklington Corp. Inc. with a par value of, and which are redeemable at, U.S. $100 per share and which carry annual non-cumulative dividends of U.S. $11 per share. In November 1989, a demand for redemption of the shares was made by Gainers Inc. and an action was commenced against Mr. Peter Pocklington arising from this investment, seeking by way of damages the monies invested together with interest thereon. Mr. Pocklington has counterclaimed seeking statutory indemnification as a director for his actions. Management believes that this counterclaim is without merit. Final determination of the realizable value of the investment is subject to the outcome of the various actions. The investment in Pocklington Corp. Inc. has been written down to $0 on the balance sheet.

Advances to the former affiliate are non-interest bearing and have no specific terms of repayment. In January 1990, Gainers Inc. made demand on and brought an action against Pocklington Financial Corporation (formerly Pocklington Holdings Inc.) to recover the advances. In December 1995, a judgement was rendered and collected in favour of Gainers Inc. in the amount of $770,000. This amount has been recovered by the Company from Pocklington Financial Corporation. This amount is subject to the secured claim of the Province as described in Note 5. The Company has appealed this decision as the Company believes that the amount of the judgement should have been higher. The outcome of the appeal is not currently determinable.

On August 8, 1989, Gainers Inc. acquired the shares of 350151 Alberta Ltd. ("350151") for $100 cash. On October 4, 1989, Gainers Inc., at the direction of the former owner, sold the shares of 350151 to Pocklington Holdings Inc. for $100 cash. The Province of Alberta ("Alberta") is attempting to have the sale reversed. The accounts of 350151 are not included in these accounts. In December 1995, a judgement as to the ownership of the shares was rendered in favour of Pocklington Financial Corporation. The Province has appealed this decision.

Note 3 Other assets

The two defined benefit plans of the Company, being Gainers Inc. Salaried Employees' Pension Plan and Gainers Inc. Hourly Pension Plan (locations other than Edmonton), were wound up in the prior year. The liabilities of the plans have been fully discharged and the surplus from the pension plans has been recovered by Gainers Inc. The surplus is subject to a secured charge and claim by the Province and was paid to the Province in the current year.

Note 4 Income taxes

The Company has capital and non-capital income tax losses available for carry forward to reduce taxable income of future years.

Note 5 Long-term debt

| | September 30 1998 | September 27 1997 |
|---|---|---|
| Province of Alberta | | |
| Term loan, originally payable by semi-annual instalments commencing April 1, 1991 of $964,650 principal and interest; interest at 9.6% | $ 6,000 | $ 6,000 |
| Assignment of prior operating loans from previous banker | | |
| Term bank loan (U.S. $8,749,339), interest at prime plus 1-1/2% | 11,567 | 11,567 |
| Operating loan, interest at prime plus 1-1/2% | 20,979 | 20,979 |
| Manual loan | 5,000 | 5,000 |
| Advances under guarantee for principal and interest payments | 31,947 | 31,947 |
| Promissory note, interest at prime plus 3% | 49,000 | 49,000 |
| Advance to facilitate sale | 13,000 | 13,000 |
| Advances under guarantee and indemnity for operating line | 18,469 | 18,469 |
| Default costs and guarantee fees, interest at prime plus 3% | 11,060 | 9,525 |
| Accrued interest | 34,491 | 34,491 |
| | $ 201,513 | $ 199,978 |

The fair value of the long-term debt is dependent on outcomes from claims filed by or against Gainers Inc. and recoveries from the sale of fixed assets. Due to the uncertainty of these items, the fair value as at September 30, 1998 is estimated to be $nil.

Province of Alberta

On September 25, 1987, Gainers Inc. and GPI entered into the Master Agreement with Alberta which provided for a term loan facility and a loan guarantee. Pursuant to the Master Agreement, Gainers Inc. and GPI granted securities to 369413 Alberta Ltd. ("Nominee") which holds the securities and loans, as later described in this Note, in trust for Alberta. A number of events of default, which still continue, occurred during 1989, resulting in the long-term debt and liability to Alberta becoming due and payable. Alberta acted on its security and, on October 6, 1989, took control of Gainers Inc.'s issued and outstanding shares which, previous to this, were controlled by Mr. Peter Pocklington.

As at October 6, 1989, operating loans of $20,979,000 and a term loan of U.S. $8,749,000 were transferred and assigned to the Nominee. In addition, Alberta has made payments since October 6, 1989 of $87,422,000 under the guarantee to cover principal and interest payments due, including the purchase in December 1993 of the balance due under the promissory note.

Interest

The interest on the loans and other indebtedness owing to Alberta has not been paid in accordance with the terms of the indebtedness. Effective February 5, 1994, Alberta declared all indebtedness owing by the Company to Alberta to be non-interest bearing from the later of February 5, 1994 and the date the indebtedness to the Province of Alberta was incurred.

Security

Collateral security for the indebtedness to Alberta includes a general assignment of book debts, general security agreements over all real and personal property of the Company, a pledge of inventory, and fixed and floating charge debentures amounting to $70,000,000 covering all of the assets of the Company. The Company continues to be in default and in breach of certain covenants of this indebtedness.

### Master Agreement

The Master Agreement provided for Alberta to advance a term loan to GPI in the aggregate amount of $12,000,000. As at September 30, 1989, $6,000,000 of the term loan had been advanced. An interest payment due on October 1, 1989 was not made and Alberta, acting on its security, seized control of the Company. Since default has occurred under the Master Agreement, the entire amount of the monies advanced for the term loan are due and owing by GPI to Alberta. The term loan which has been advanced, and interest thereon, and the performance and observance of the other covenants of GPI under the Master Agreement, including the obligations of GPI to Alberta in respect to the promissory note, is collaterally secured by a demand debenture made by GPI to the Nominee in the principal sum of $67,000,000 dated September 25, 1987 and constituting a fixed mortgage and charge over all of the real property, equipment and chattels of GPI and a floating charge over all of the undertaking and other property and assets of GPI, and by a pledge by GPI of preferred shares held by GPI in Gainers Inc.

## Note 6 Share capital

| | September 30 1998 | September 27 1997 |
|---|---|---|
| Authorized | | |
| Unlimited number of Class A common shares | | |
| Unlimited number of Class B preferred shares redeemable/retractable at $1 per share with non-cumulative annual dividends at a rate not exceeding 16% of the redemption value | | |
| 12,000,000 Class C preferred shares redeemable at $1 per share with cumulative annual dividend compounded semi-annually at 9.6% of the redemption price | | |
| Issued | | |
| 101 Class A common shares | $ 1 | $ 1 |
| 6,000,000 Class C preferred shares | 6,000 | 6,000 |
| | 6,001 | 6,001 |
| Less: 6,000,000 Class C preferred shares held by GPI | 6,000 | 6,000 |
| | $ 1 | $ 1 |

## Note 7 Contingencies

(a) The Company and Alberta have filed claims against Mr. Peter Pocklington and companies controlled by him for recovery of certain loans, payments and other transactions prior to October 6, 1989. The claim aggregates approximately $38,000,000 plus interest. Ultimate recovery of this claim cannot be determined at this time.

(b) Under the terms of the Master Agreement, the Company and Mr. Peter Pocklington are liable for all losses, expenses, costs and claims incurred by Alberta as a consequence of a default by GPI or by any other member of the group of Mr. Pocklington. As a result, since the date of default the Company has provided approximately $11,060,000 in the consolidated financial statements for these costs and expenses. It is expected that further costs and expenses will be incurred in the future as a result of continuing default. Ultimate recovery of this claim cannot be determined at this time.

(c) During 1991, an employee filed a claim for damages for constructive dismissal in the amount of $520,000 and damages for breach of contract in the amount of $2,000,000, plus interest and costs against Gainers Inc. Gainers Inc. defended the action and brought a third-party claim against Mr. Peter Pocklington for any damages payable by Gainers Inc. to the employee. The employee's claim was dismissed by the Court and the Court awarded costs to Gainers Inc. The employee has filed an appeal of this decision, but counsel advises that there is little likelihood that the appeal will proceed or will be successful.

(d) Alberta has brought a claim against Mr. Peter Pocklington for $4 million plus interest and costs. Mr. Peter Pocklington has brought a counter claim against the Company in which Mr. Pocklington claims indemnification for the entire amount of the main claim.

Note 8 Uncertainty due to the Year 2000 Issue

The Year 2000 Issue arises because many computerized systems use two digits rather than four to identify a year. Date-sensitive systems may recognize the year 2000 as 1900 or some other date, resulting in errors when information using year 2000 dates are processed. In addition, similar problems may arise in some systems, which use certain dates in 1999 to represent something other than a date. The effects of the Year 2000 Issue may be experienced before, on, or after January 1, 2000, and, if not addressed, the impact on operations and financial reporting may range from minor errors to significant systems failure, which could affect an entity's ability to conduct normal business operations. It is not possible to be certain that all aspects of the Year 2000 Issue affecting the entity, including those related to the efforts of customers, suppliers, or other third parties, will be fully resolved.

Note 9 Comparative figures

Certain comparative figures have been reclassified to conform with the current year's presentation.

## STATEMENT OF REMISSIONS, COMPROMISES AND WRITE-OFFS
## FOR THE YEAR ENDED MARCH 31, 1999

The following statement has been prepared pursuant to section 28 of the Financial Administration Act. The statement includes all remissions, compromises and write-offs of the Ministry of Treasury made or approved during the fiscal year.

| | |
|---|---|
| Remissions under section 26 of the Financial Administration Act: | |
| Department of Treasury: | |
| Chembiomed Ltd. | $ 22,659,703 |
| Fuel Tax Act | 5,510,651 |
| Alberta Corporate Tax Act | 57,979 |
| Alberta Income Tax Act | 15,986 |
| | 28,244,319 |
| Compromises under section 27 of the Financial Administration Act: | |
| Alberta Heritage Savings Trust Fund: | |
| Alberta Pacific Pulp Mill Project | 114,220,018 |
| Write-offs: | |
| Department of Treasury: | |
| Implemented guarantees and indemnities: | |
| Credit Union Deposit Guarantee Corporation | 14,491,698 |
| North Saskatchewan River Boat Ltd. | 500,000 |
| Farm Credit Stability Act | 419,217 |
| Small Business Term Assistance Act | 143,187 |
| Canadian Western Bank | 44,861 |
| Family First Home Program | 10,319 |
| | 15,609,282 |
| Accounts receivable | 2,052,139 |
| | 17,661,421 |
| Alberta Treasury Branches: | |
| Accounts and loans receivable | 46,391,537 |
| Credit Union Deposit Guarantee Corporation: | |
| Accounts receivable | 1,920 |
| | 64,054,878 |
| | $ 206,519,215 |

## STATEMENT OF BORROWINGS MADE UNDER SECTION 61(1) OF THE FINANCIAL ADMINISTRATION ACT FOR THE YEAR ENDED MARCH 31, 1999

| | Issue Principal | Proceeds |
|---|---|---|
| Payable in Canadian dollars: | | |
| Promissory notes | $ 19,659,200,000 | $ 19,609,682,532 |
| Debentures | 900,000,000 | 886,865,000 |
| | $ 20,559,200,000 | $ 20,496,547,532 |
| Payable in U.S. dollars: | | |
| Promissory notes | $ 2,256,716,020 | $ 2,247,512,296 |
| Debentures | 1,233,000,000 | 1,226,325,405 |
| | $ 3,489,716,020 | $ 3,473,837,701 |

## STATEMENT OF THE AMOUNT OF THE DEBT OF THE CROWN FOR WHICH SECURITIES WERE PLEDGED

The following statement has been prepared pursuant to section 68(2) of the Financial Administration Act.

The amount of the debt of the Crown outstanding at the end of the 1998-99 fiscal year for which securities were pledged under Part 6 of the Financial Administration Act was $nil.

## STATEMENT OF GUARANTEES AND INDEMNITIES
## FOR THE YEAR ENDED MARCH 31, 1999

The following statement has been prepared pursuant to section 76 of the Financial Administration Act. The statement summarizes the amounts of all guarantees and indemnities given by the Ministry of Treasury on behalf of the Crown and Provincial corporations for the year ended March 31, 1999, the amounts paid as a result of liability under guarantees and indemnities, and the amounts recovered on debts owing as a result of payments under guarantees and indemnities.

| Program Borrower | Amount of Guarantee or Indemnity | Payments | Recoveries |
|---|---|---|---|
| CROWN GUARANTEES | | | |
| Gainers Inc. and subsidiaries | $ - | $ 2,486,406 | $ 2,916,096 |
| North Saskatchewan River Boat Ltd. | - | 500,000 | - |
| Farm Credit Stability Act | - | 419,217 | - |
| Small Business Term Assistance Act | - | 143,187 | 4,367 |
| Rural utilities loans | 1,017,565 | 2,789 | 15,845 |
| Feeder Associations Guarantee Act | 2,525,000 | | - |
| Judgement debts | - | - | 29,777 |
| | 3,542,565 | 3,551,599 | 2,966,085 |
| CROWN INDEMNITIES | | | |
| Credit Union Deposit Guarantee Corporation | - | 14,491,698 | |
| Canadian Western Bank | - | 41,342 | - |
| | - | 14,533,040 | - |
| PROVINCIAL CORPORATION GUARANTEES/INDEMNITIES | | | |
| Alberta Securities Commission | 2,160,000 | - | - |
| N.A. Properties (1994) Ltd. | 615,000 | - | - |
| | 2,775,000 | - | - |
| | $ 6,317,565 | $ 18,084,639 | $ 2,966,085 |

LOCAL AUTHORITIES PENSION PLAN
FINANCIAL STATEMENTS
DECEMBER 31, 1998



## AUDITOR'S REPORT

To the Local Authorities Pension Plan
Board of Trustees

I have audited the statement of net assets available for benefits and accrued benefits of the Local Authorities Pension Plan as at December 31, 1998 and the statements of changes in net assets available for benefits, changes in accrued benefits and changes in actuarial surplus for the year then ended. These financial statements are the responsibility of the Plan's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In my opinion, these financial statements present fairly, in all material respects, the financial position of the Plan as at December 31, 1998 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles.

Peter Valentine, FCA
Auditor General

Edmonton, Alberta
June 24, 1999

# LOCAL AUTHORITIES PENSION PLAN
## STATEMENT OF NET ASSETS AVAILABLE FOR BENEFITS AND ACCRUED BENEFITS
### As at December 31, 1998
($ thousands)

| | 1998 | 1997 |
|---|---|---|
| **Net Assets Available for Benefits** | | |
| Assets | | |
| Investments (Note 3) | $ 7,640,969 | $ 7,207,464 |
| Accrued investment income | 1,369 | 3,148 |
| Contributions receivable (Note 6) | 10,617 | 9,577 |
| Receivable from Province of Alberta | - | 283 |
| | 7,652,955 | 7,220,472 |
| Liabilities | | |
| Due to TELUS Edmonton (Note 7) | - | 158,290 |
| Accounts payable (Note 8) | 3,840 | 2,375 |
| | 3,840 | 160,665 |
| Net assets available for benefits | 7,649,115 | 7,059,807 |
| Actuarial asset fluctuation reserve (Note 9) | (200,300) | (373,200) |
| Actuarial value of net assets available for benefits | 7,448,815 | 6,686,607 |
| **Accrued Benefits** | | |
| Actuarial value of accrued benefits (Note 13) | 6,943,400 | 6,324,100 |
| Actuarial surplus (Notes 9 and 13) | $ 505,415 | $ 362,507 |

See accompanying notes and schedules.

# LOCAL AUTHORITIES PENSION PLAN
## STATEMENT OF CHANGES IN NET ASSETS AVAILABLE FOR BENEFITS
### For the year ended December 31, 1998
($ thousands)

| | 1998 | 1997 |
|---|---|---|
| Increase in assets | | |
| Investment income (Note 10) | $ 638,154 | $ 789,048 |
| Contributions (Note 11) | 260,977 | 286,847 |
| Total increase in assets | 899,131 | 1,075,895 |
| Decrease in assets | | |
| Pension benefits | 263,794 | 251,738 |
| Transfer to TELUS Edmonton (Note 7) | 579 | 158,290 |
| Refunds to members | 36,605 | 40,092 |
| Transfers to other plans | 376 | 611 |
| Interest on refunds of additional contributions | 429 | - |
| Administration expenses (Note 12) | 8,040 | 5,746 |
| Total decrease in assets | 309,823 | 456,477 |
| Increase in net assets for the year | 589,308 | 619,418 |
| Net assets available for benefits at beginning of year | 7,059,807 | 6,440,389 |
| Net assets available for benefits at end of year | $ 7,649,115 | $ 7,059,807 |

See accompanying notes and schedules.

## LOCAL AUTHORITIES PENSION PLAN
## STATEMENT OF CHANGES IN ACCRUED BENEFITS
### For the year ended December 31, 1998
($ thousands)

| | Year ended December 31, 1998 | | | Year ended December 31, 1997 |
|---|---|---|---|---|
| | Pre-1992 | Post-1991 | Total | Total |
| Increase in accrued benefits | | | | |
| Interest accrued on benefits | $ 355,200 | $ 120,300 | $ 475,500 | $ 469,200 |
| Changes in actuarial assumptions (Note 13) | 151,100 | 78,500 | 229,600 | 177,900 |
| Benefits earned | - | 270,800 | 270,800 | 259,300 |
| Increase in accrued benefits | 506,300 | 469,600 | 975,900 | 906,400 |
| Decrease in accrued benefits | | | | |
| Benefits paid including interest | 269,800 | 40,700 | 310,500 | 292,500 |
| Experience gains (losses) | 34,300 | 13,100 | 47,400 | (2,100) |
| Transfer to TELUS Edmonton | (1,000) | (300) | (1,300) | 138,300 |
| Decrease in accrued benefits | 303,100 | 53,500 | 356,600 | 428,700 |
| Net increase in accrued benefits | 203,200 | 416,100 | 619,300 | 477,700 |
| Accrued benefits at beginning of year | 4,722,100 | 1,602,000 | 6,324,100 | 5,846,400 |
| Accrued benefits at end of year (Note 13) | $ 4,925,300 | $ 2,018,100 | $ 6,943,400 | $ 6,324,100 |

See accompanying notes and schedules.

## LOCAL AUTHORITIES PENSION PLAN
## STATEMENT OF CHANGES IN ACTUARIAL SURPLUS
### For the year ended December 31, 1998
($ thousands)

| | Year ended December 31, 1998 | | | Year ended December 31, 1997 |
|---|---|---|---|---|
| | Pre-1992 | Post-1991 | Total | Total |
| Actuarial surplus at beginning of year as originally reported | $ 48,200 | $ 489,807 | $ 538,007 | $ 163,789 |
| Actuarial asset fluctuation reserve (Note 9) | (132,900) | (42,600) | (175,500) | - |
| Actuarial surplus at beginning of year as restated | (84,700) | 447,207 | 362,507 | 163,789 |
| Net increase in net assets available for benefits | 176,000 | 413,308 | 589,308 | 619,418 |
| Net decrease in actuarial asset fluctuation reserve | 139,700 | 33,200 | 172,900 | 232,500 |
| Net increase in accrued benefits | (203,200) | (416,100) | (619,300) | (477,700) |
| Actuarial surplus at end of year | $ 27,800 | $ 477,615 | $ 505,415 | $ 538,007 |

See accompanying notes and schedules

# LOCAL AUTHORITIES PENSION PLAN
# NOTES TO THE FINANCIAL STATEMENTS
# DECEMBER 31, 1998

Note 1 Summary Description of the Plan

The following description of the Local Authorities Pension Plan is a summary only. For a complete description of the plan, reference should be made to the *Public Sector Pension Plans Act*, Chapter P-30.7, Statutes of Alberta 1993 and Alberta Regulation 366/93.

(a) General

The Local Authorities Pension Plan is a contributory defined benefit pension plan for eligible employees of local authorities and approved public bodies. These include cities, towns, villages, municipal districts, hospitals, school divisions and districts, colleges and technical institutes.

(b) Funding

Current service costs are funded by employers and employees at rates which are expected to provide for all benefits payable under the plan. The rates in effect at December 31, 1998 for employees are 4.025% of pensionable earnings up to the Canada Pension Plan's Year's Maximum Pensionable Earnings (YMPE) and 5.90% for the excess. The rates in effect for employers are 1.0% more than the rates for employees. The rates are to be reviewed at least once every three years by the board based on recommendations of the plan's actuary.

(c) Retirement Benefits

The plan provides for a pension of 1.4% for each year of pensionable service based on the average salary of the highest five consecutive years up to the YMPE and 2.0% on the excess. The maximum service allowable under the plan is 35 years. Unreduced pensions are payable to members who retire with at least five years of service and have either attained age 65 or age 55 and the sum of their age and service equals 85. Reduced pensions are payable to members retiring early.

(d) Disability Benefits

Pensions are payable to members who become totally disabled and retire early with at least five years of service. Reduced pensions are payable to members who become partially disabled and retire early with at least five years of service.

(e) Death Benefits

Death benefits are payable on the death of a member if the member had at least five years of service. The benefits may take the form of a survivor pension, if the beneficiary is a spouse, or a lump sum payment. The beneficiary of a deceased member with fewer than five years of service is entitled to receive death benefits in the form of a lump sum payment.

(f) Termination Benefits

Members who terminate with at least five years of service and who are not immediately entitled to a pension may receive a refund of contributions and interest on service prior to 1992 and the commuted value for service after 1991, which is subject to lock-in provisions. Alternatively, they may elect to receive a deferred pension. Members who terminate with fewer than five years of service receive a refund of their contributions and interest.

(g) Prior Service and Reciprocal Transfers

All prior service purchases are to be cost-neutral to the plan.

Transferred-in service will be on an actuarial reserve basis and transfers out will receive the greater of the termination benefits or commuted value for all service.

(h) Cost-of-Living Adjustments

Pensions payable are increased each year by an amount equal to 60% of the increase in the Alberta Consumer Price Index.

(i) Income Taxes

The plan is a registered pension plan as defined in the *Income Tax Act*. The plan's registration number is 0216556.

Note 2 Summary of Significant Accounting Policies and Reporting Practices

(a) Basis of Presentation

These financial statements are prepared on the going concern basis in accordance with generally accepted accounting principles. The statements provide information about the net assets available in the plan to meet future benefit payments and are prepared to assist plan members and others in reviewing the activities of the plan for the year. They do not reflect the funding requirements of the plan or the benefit security of individual participants.

The majority of plan investments are held in pooled investment funds administered by Alberta Treasury. Pooled investment funds have a market-based unit value that is used to allocate income to participants and to value purchases and sales of pool units.

The plan's percentage ownership in pooled investment funds at December 31 was as follows:

| | % Ownership | |
|---|---|---|
| | 1998 | 1997 |
| Canadian Dollar Public Bond Pool | 35.1 | 36.8 |
| Canadian Pooled Equities Fund | 49.2 | 51.1 |
| Domestic Passive Equity Pooled Fund | 45.1 | - |
| External Managers Fund | 38.2 | 41.9 |
| Global Structured Equity Pooled Fund | 31.3 | 42.1 |
| Private Bond Pool | 41.2 | 39.4 |
| Private Equity Pool | 53.3 | 47.5 |
| Private Mortgage Pool | 39.4 | 39.6 |
| Private Real Estate Pool | 40.6 | 40.3 |
| Transition Account | 58.7 | - |
| United States Pooled Equities Fund | 39.7 | 42.1 |
| US Passive Equity Pooled Fund | 37.6 | - |

(b) Valuation of Assets and Liabilities

Investments are stated at fair value. The methods used to determine fair value of investments held either by the plan or by pooled investment funds are explained in the following paragraphs.

Short-term securities, public fixed income securities and equities are valued at the year-end closing sale price or the average of the latest bid and ask prices quoted by an independent securities valuation company.

Private fixed income securities and mortgages are valued based on the net present value of future cash flows. These cash flows are discounted using Government of Canada bond rates adjusted for a risk premium estimated by management.

The fair value of private equities is estimated by management.

Real estate investments are reported at their most recent appraised value net of any liabilities against the real property. Real estate properties are appraised annually by qualified external real estate appraisers.

The fair values of deposits, receivables, accrued investment income and payables are estimated to approximate their book values.

(c) Actuarial Value of Net Assets Available for Benefits

To reduce the potential volatility in the plan's funded status due to the effects of market fluctuations on investments, asset values are adjusted by an actuarial asset fluctuation reserve. Assets are projected to increase at the rate of return assumed in the actuarial valuation. The actuarial value of assets is determined by averaging actual and projected asset values over three years.

(d) Income Recognition

Dividends are accrued on the ex-dividend date. Income from other investments is accrued as earned. Gains or losses on investments are recognized concurrently with changes in fair value.

(e) Foreign Exchange

Foreign currency transactions are translated into Canadian dollars using average rates of exchange except for hedged foreign currency transactions, which are translated at rates of exchange established by the terms of the forward exchange contracts. At the year-end, the fair value of investments and any other assets and liabilities denominated in a foreign currency are translated at the year-end exchange rate. Exchange differences are included in the determination of investment income.

(f) Derivative Financial Instruments

Income and expense on index swaps and interest rate swaps are accrued as earned and included in investment income. Gains and losses on forward foreign exchange contracts are recognized concurrently with changes in fair value. As explained in Notes 4 and 5, controls are in place respecting the use of derivatives.

Note 3 Investments (Schedules A to D)

Investments are summarized as follows:

| | 1998 | | 1997 | |
|---|---|---|---|---|
| | ($ thousands) | % | ($ thousands) | % |
| Deposit in the Consolidated Cash | | | | |
| Investment Trust Fund (a) | $ 101,155 | 1.3 | $ 111,874 | 1.5 |
| Fixed Income Securities | | | | |
| Canadian Dollar Public Bond Pool | | | | |
| (Schedule A) | 2,903,372 | 38.0 | 2,577,156 | 35.8 |
| Private Mortgage Pool (b) | 364,386 | 4.8 | 310,089 | 4.3 |
| Real Rate of Return Bonds (c) | 51,803 | 0.6 | 119,340 | 1.7 |
| Private Bond Pool | 665 | - | 169,298 | 2.3 |
| Government of Canada, direct | - | - | 50,409 | 0.7 |
| Total deposits and fixed income securities | 3,421,381 | 44.7 | 3,338,166 | 46.3 |
| Canadian Equities | | | | |
| Canadian Pooled Equities Fund (Schedule B) | 868,092 | 11.4 | 1,874,769 | 26.0 |
| Transition Account and miscellaneous | 753 | - | - | - |
| Domestic Passive Equity Pooled Fund | | | | |
| (Schedule C) | 854,275 | 11.2 | - | - |
| External Managers Fund (Canadian) (Schedule D) | 401,855 | 5.3 | 175,297 | 2.4 |
| Private Equity Pool (d) | 50,913 | 0.6 | 57,495 | 0.8 |
| Passive Index Fund | - | - | 32,560 | 0.5 |
| Foreign Equities | | | | |
| External Managers Fund (Global) (Schedule D) | 933,679 | 12.2 | 754,103 | 10.5 |
| Global Structured Equity Pooled Fund (e) | 423,732 | 5.5 | 351,671 | 4.9 |
| US Passive Equity Pooled Fund (f) | 228,615 | 3.0 | - | - |
| External Managers Fund (United States) | | | | |
| (Schedule D) | 225,552 | 3.0 | 166,140 | 2.3 |
| United States Pooled Equities Fund | 6,351 | 0.1 | 274,040 | 3.8 |
| Equities in Real Estate | | | | |
| Private Real Estate Pool (g) | 225,771 | 3.0 | 183,223 | 2.5 |
| Total equities | 4,219,588 | 55.3 | 3,869,298 | 53.7 |
| Total Investments | $ 7,640,969 | 100.0 | $ 7,207,464 | 100.0 |

(a) The Consolidated Cash Investment Trust Fund is managed with the objective of providing competitive interest income to depositors while maintaining maximum security and liquidity of depositors' capital. The portfolio is comprised of high quality short-term and mid-term fixed income securities with a maximum term to maturity of five years.

(b) The Private Mortgage Pool is managed with the objective of providing investment returns higher than attainable from the publicly traded bond market over the long term. The portfolio is comprised primarily of high-quality commercial mortgage loans. In order to reduce risk, the pool only invests in loans insured by a federal agency and first-mortgage loans that provide diversification by property usage. The pool does not invest in mortgages on single family houses, hotels, motels, trailer parks or recreational properties. As at December 31, 1998, mortgages held by the pool have an average effective yield of 6.92% per annum based on market (1997: 7.64% per annum). Approximately 90% of the mortgages held will mature within ten years (1997: 91%).

(c) Real rate of return bonds are issued or guaranteed by the Government of Canada, bear interest at a fixed rate adjusted for inflation and have terms to maturity of over 20 years.

(d) The Private Equity Pool is managed with the objective of providing investment returns higher than attainable from the publicly traded equity indices such as the Toronto Stock Exchange 300 Index over the long term. The portfolio is comprised of equity investments in companies that show higher than average growth potential. Risk is reduced by avoiding direct investments in start-up and venture capital situations and by limiting holdings in any single company.

(e) The Global Structured Equity Pooled Fund is managed with the objective of providing investment returns comparable to the total return of the Morgan Stanley Capital International World Index. The pooled fund provides exposure to global markets through the use of structured investments such as foreign equity index swaps and interest rate swaps. All payments and receipts relating to swaps are in Canadian dollars. Participation in the pooled fund qualifies as a Canadian investment under the *Income Tax Act*.

(f) The US Passive Equity Pooled Fund is managed with the objective of attaining investment returns comparable to Standard & Poor's (S & P) 500 Total Return Index over a four-year period. The portfolio is comprised of publicly traded equities in the United States similar in weights to the S & P 500 Index. To enhance investment returns with no substantial increase in risks, the pooled fund also invests in futures, swaps and other structured investments.

(g) The Private Real Estate Pool is managed with the objective of providing investment returns comparable to the Russell Canadian Property Index over the long term. Real estate is held through intermediate companies, which have issued to the pool common shares and participating debentures secured by a charge on real estate. Risk is reduced by investing in properties that provide diversification, by geographic location, by property type and by tenancy. As real estate returns are positively correlated to inflation and negatively correlated to returns from fixed income securities and equities, the pool provides diversification from the securities market.

Note 4 Investment Risk Management

Fair values of investments are exposed to credit risk and price risk. Credit risk relates to the possibility that a loss may occur from the failure of another party to perform according to the terms of a contract. Price risk is comprised of currency risk, interest rate risk and market risk. Currency risk relates to the possibility that the investments will change in value due to future fluctuations in foreign exchange rates. Interest rate risk relates to the possibility that the investments will change in value due to future fluctuations in market interest rates. Market risk relates to the possibility that the investments will change in value due to future fluctuations in market prices.

Actuarial liabilities of the plan are primarily affected by the long-term real rate of return on investments. In order to earn the best possible return at an acceptable level of risk, the Board of Trustees established a policy asset mix of 30% to 50% fixed income instruments and 50% to 70% equities. Investment risk is reduced through asset class diversification, diversification within each asset class, quality constraints on fixed income instruments and restrictions on amounts exposed to countries designated as emerging markets. Borrowing or leveraging is not allowed with the exception of pre-existing mortgages on real estate properties. Controls are in place respecting the use of derivatives (see Note 5). Forward foreign exchange contracts are used to manage currency exposure in connection with securities purchased in foreign currency (see Note 5).

Note 5 Derivatives: Index Swaps, Interest Rate Swaps and Foreign Exchange Contracts

Pooled funds use index and interest rate swaps to enhance return and for hedging risks. A swap is a contractual agreement between two parties to exchange a series of cash flows based on a notional amount and does not involve the exchange of the underlying principal. An index swap involves the exchange of a floating interest rate cash flow for one based on the performance of a market index. For interest rate swaps, parties generally exchange fixed and floating rate interest cash flows based on a notional value. There are underlying securities supporting all swaps. Leveraging is not allowed.

The following is a summary of the plan's proportionate share of the current and contractual notional value of index and interest rate swaps held or issued by pooled funds at December 31, 1998:

| | 1998 | 1997 |
|---|---|---|
| | ($ thousands) | |
| Index swaps | | |
| Foreign equities | | |
| Global Structured Equity Pooled Fund | $ 395,438 | $ 276,930 |
| US Passive Equity Pooled Fund | 228,691 | - |
| Canadian equities - Domestic Passive Equity Pooled Fund | 346,820 | - |
| Bonds - Canadian Dollar Public Bond Pool | 531,457 | 354,809 |
| Interest rate swaps | | |
| Fixed to floating rates | | |
| Canadian Dollar Public Bond Pool | 356,154 | 145,750 |
| Domestic Passive Equity Pooled Fund | 236,640 | - |
| Global Structured Equity Pooled Fund | 264,371 | 236,160 |
| US Passive Equity Pooled Fund | 21,286 | - |
| Total | $ 2,380,857 | $ 1,013,649 |

Fair values of swaps have been included in the determination of the fair values of the respective pooled investment funds. Credit exposure relating to swaps is minimal as management deals only with counter-parties rated not less than AA.

Foreign exchange contracts are contractual agreements to exchange specified currencies at an agreed upon exchange rate and on an agreed settlement date in the future. As at December 31, 1998, the plan's proportionate share of outstanding forward foreign exchange contracts issued by the External Managers Fund amounted to $180,365,000 (1997: $155,139,000).

Note 6 Contributions Receivable

| | 1998 | 1997 |
|---|---|---|
| | ($ thousands) | |
| Employers | $ 5,737 | $ 4,639 |
| Employees | 4,880 | 4,015 |
| Province of Alberta | - | 923 |
| | $ 10,617 | $ 9,577 |

Note 7 Due to and Transfer to TELUS Edmonton

In December 1997, the Lieutenant Governor in Council approved the withdrawal of all active members of TELUS Edmonton from the plan effective December 31, 1997. Accordingly the plan's actuary determined that assets totalling $158,290,000 were required to be transferred to the TELUS Edmonton Pension Plan Fund. The amount was calculated in accordance with provisions of the *Public Sector Pension Plans Act, Alberta Regulation 475/97* and actuarial assumptions approved by the board for the actuarial valuation as at December 31, 1997.

In December 1998, due to data changes arising from TELUS' review of data used in the original calculation, the plan's actuary revised the amount of total assets required to be transferred to TELUS to $157,190,000. The revised amount plus an adjustment for the market return of the plan from December 31, 1997 to the date of transfer totalling $158,869,000 were transferred to the TELUS Edmonton Pension Plan Fund in 1998. All rights of TELUS Edmonton and its employees in relation to the plan are extinguished.

Note 8 Accounts Payable

| | 1998 | 1997 |
|---|---|---|
| | ($ thousands) | |
| Benefits | $ 68 | $ 67 |
| Refunds and transfers | 1,534 | 2,308 |
| Additional contribution refunds and accrued interest | 1,507 | - |
| Administration expenses | 731 | - |
| | $ 3,840 | $ 2,375 |

Note 9 Change in Actuarial Value of Net Assets Available for Benefits

Investments held by the plan are stated at fair value as at December 31, 1998. In order to minimize contribution instability and the effects of market volatility on asset values, the actuarial value of assets has been determined by adjusting assets by an actuarial asset fluctuation reserve. The method of determining the actuarial value of net assets available for benefits has been changed from that used in 1996 and 1997 on the recommendations of the plan's actuary. Prior to 1998, the adjustment was determined by amortizing annual net unrealized gains and losses equally over three years. In 1998, asset values are projected to increase at the rate of return assumed in the actuarial valuation. The actuarial value of assets is determined by averaging actual and projected asset values over three years. The actuarial asset fluctuation reserve is the difference between the actuarial value of assets and actual asset value. As with the accrued benefits, the actuarial asset fluctuation reserve has been allocated between the pre-1992 and post-1991 periods.

The actuarial asset fluctuation reserve for 1997 has been restated to reflect this change in accounting method. The change in method has the effect of reducing the actuarial value of net assets available for benefits and actuarial surplus by $101.1 million in 1998 (1997: $175.5 million). If the change had not been made, the actuarial surplus of the plan would have been $606.5 million as at December 31, 1998 (1997: $538.0 million).

Note 10 Investment Income

| | 1998 | | | 1997 |
|---|---|---|---|---|
| | Income (a) | Change in Fair Value | Total | Total |
| | ($ thousands) | | | |
| Deposits and Fixed Income Securities: | | | | |
| Deposit in the Consolidated Cash Investment Trust Fund | $ 5,295 | $ - | $ 5,295 | $ 3,648 |
| Canadian Dollar Public Bond Pool | 171,530 | 58,548 | 230,078 | 231,434 |
| Private Mortgage Pool | 29,561 | 4,772 | 34,333 | 22,765 |
| Real Rate of Return Bonds | 5,573 | 3,902 | 9,475 | 5,456 |
| Private Bond Pool | 17,215 | (600) | 16,615 | 7,670 |
| Public, direct | 505 | 14 | 519 | 1,701 |
| | 229,679 | 66,636 | 296,315 | 272,674 |
| Equities: | | | | |
| Canadian Pooled Equities Fund | 22,472 | (54,736) | (32,264) | 246,991 |
| Transition Account and miscellaneous | 16,763 | 89,531 | 106,294 | - |
| Domestic Passive Equity Pooled Fund | (27,702) | (104,654) | (132,356) | - |
| External Managers Fund (Canadian) | 2,168 | (3,933) | (1,765) | 32,342 |
| Private Equity Pool | 949 | (1,476) | (527) | 4,616 |
| Passive Index Fund | 149 | - | 149 | 360 |
| External Managers Fund (Global) | 13,191 | 185,213 | 198,404 | 40,001 |
| Global Structured Equity Pooled Fund | 71,155 | 906 | 72,061 | 44,482 |
| US Passive Equity Pooled Fund | 35,410 | 14,949 | 50,359 | - |
| External Managers Fund (United States) | 1,396 | 64,619 | 66,015 | 49,582 |
| United States Pooled Equities Fund | 14 | (9,983) | (9,969) | 67,047 |
| Private Real Estate Pool | 10,286 | 15,152 | 25,438 | 30,953 |
| | 146,251 | 195,588 | 341,839 | 516,374 |
| | $ 375,930 | $ 262,224 | $ 638,154 | $ 789,048 |

(a) Income is comprised of dividends, interest and rental income.

Note 11 Contributions

| | 1998 | 1997 |
|---|---|---|
| | ($ thousands) | |
| Current and prior service | | |
| Employers | $ 140,946 | $ 134,776 |
| Employees (a) | 119,829 | 114,993 |
| Pre-1992 unfunded liability | | |
| Employers | (90) | 12,790 |
| Employees | (90) | 12,790 |
| Province of Alberta | (77) | 10,963 |
| Transfers from other plans and miscellaneous | 459 | 535 |
| | $ 260,977 | $ 286,847 |

(a) Includes $4,805,000 (1997: $5,757,000) of prior service contributions.

Note 12 Administration Expenses

| | 1998 | 1997 |
|---|---|---|
| | ($ thousands) | |
| General administration costs | $ 6,284 | $ 4,825 |
| Investment management costs | 1,036 | 743 |
| Plan restructuring costs (to move LAPP to independence) | 627 | - |
| Actuarial fees | 93 | 178 |
| | $ 8,040 | $ 5,746 |

General administration costs including board costs were paid to Alberta Pensions Administration Corporation on a cost-recovery basis.

Investment management costs were paid to Alberta Treasury and do not include custodial and external management fees, which have been deducted in arriving at investment income.

Plan restructuring costs (see Note 16) include $39,612 in remuneration, comprising $35,402 in salaries and $4,210 in benefits, paid to the Chief Executive Officer of the Local Authorities Pension Plan Corporation for the period from September 28, 1998 to December 31, 1998.

Total administration expenses, excluding plan restructuring costs, amounted to $69 per member (1997: $54 per member). The $15 per member cost increase in 1998 is attributed to the following factors: changes in the accounting treatment of business process reengineering cost $8, increases in operating and plan specific cost $4, and investment management cost $3.

Note 13 Accrued Benefits

(a) Actuarial Valuation

An actuarial valuation of the plan was carried out as at December 31, 1998 by William M. Mercer Limited. The December 31, 1998 valuation resulted in an actuarial surplus of $505 million as disclosed in the statement of net assets available for benefits and accrued benefits.

The valuation as at December 31, 1998 was determined using the projected benefit method based on service. The assumptions used in the valuation were developed as the best estimate of expected market conditions and other future events. This estimate was, after consultation with the plan's actuary, adopted by the Local Authorities Pension Plan Board of Trustees. The major assumptions used were:

| | December 31 | |
|---|---|---|
| | 1998 Valuation | 1997 Valuation |
| | % | % |
| Investment return | 7.25 | 7.5 |
| Inflation rate | 3.5 | 3.5 |
| Salary escalation rate | 4.25* | 4.25* |

* Total rate plus merit and promotion.

The following table summarizes the effects of changes in major actuarial assumptions, which increase (decrease) accrued benefits at December 31, 1998:

| | 1998 | | | 1997 |
|---|---|---|---|---|
| | Pre-1992 | Post-1991 | Total | Total |
| | ($ thousands) | | | |
| Investment return | $ 151,100 | $ 78,500 | $ 229,600 | $ 430,000 |
| Inflation and salary escalation rates | - | - | - | (252,100) |
| Changes in actuarial assumptions | $ 151,100 | $ 78,500 | $ 229,600 | $ 177,900 |

In accordance with the requirements of the *Public Sector Pension Plans Act*, a separate accounting is required of the pension liability with respect to service that was recognized as pensionable as at December 31, 1991. This information is provided in the statement of changes in accrued benefits which shows the principal components of the change in the actuarial value of accrued benefits.

Based on the information provided above, the following table summarizes the accrued benefits, actuarial value of net assets and the resulting actuarial surplus at December 31, 1998:

| | 1998 | | | 1997 |
|---|---|---|---|---|
| | Pre-1992 | Post 1991 | Total | Total |
| | ($ thousands) | | | |
| Fair value of assets | $ 5,090,800 | $ 2,558,315 | $ 7,649,115 | $ 7,059,807 |
| Actuarial asset fluctuation reserve (Note 9) | (137,700) | (62,600) | (200,300) | (373,200) |
| Actuarial value of net assets | 4,953,100 | 2,495,715 | 7,448,815 | 6,686,607 |
| Accrued benefits | 4,925,300 | 2,018,100 | 6,943,400 | 6,324,100 |
| Actuarial surplus | $ 27,800 | $ 477,615 | $ 505,415 | $ 362,507 |

(b) Sensitivity of Changes in Major Assumptions

The plan's future experience will inevitably differ, perhaps significantly, from the assumptions. Any differences between the actuarial assumptions and future experience will emerge as gains or losses in future valuations and will affect the financial position of the plan.

As at December 31, 1998, holding the nominal investment return and salary escalation assumptions constant, a 1% increase in the assumed long-term inflation rate would result in a decrease in the actuarial surplus of the plan from $505 million to $74 million.

As at December 31, 1998, holding the inflation and nominal investment return assumptions constant, a 1% increase in the assumed salary escalation would result in a decrease in the actuarial surplus of the plan from $505 million to $275 million.

As at December 31, 1998, holding the inflation and salary escalation assumptions constant, a 1% increase in the assumed real long-term investment return would result in an increase in the actuarial surplus of the plan from $505 million to $1,380 million.

Note 14 Funding

Current service costs are funded by employers and employees at rates that are expected to provide for all benefits payable under the plan. The rates are to be reviewed at least once every three years by the board based on recommendations of the plan's actuary. The latest valuation as at December 31, 1998 disclosed an actuarial surplus of $28 million for pre-1992 service and $477 million for post-1991 service resulting in an actuarial surplus of $505 million for the plan.

In accordance with the provisions of the *Public Sector Pension Plans Act*, the Province of Alberta has no further liability in respect of the plan's pre-1992 unfunded liability as the plan's actuarial valuation as at December 31, 1997 shows that its unfunded liability for service prior to January 1, 1992 has been eliminated.

Note 15 Remuneration of Board Members

Remuneration paid with respect to a total of 14 board members during the year amounted to $118,000 (1997: $156,000).

Note 16 Plan Restructuring

In June 1997, the Local Authorities Pension Plan Board of Trustees approved the development of a non-statutory pension plan to replace the existing statutory plan effective the end of 1999. In accordance with provisions and regulations of the *Public Sector Pension Plans Act*, the board is authorized to charge the plan, up to a certain extent, all costs incurred in connection with the development of the non-statutory plan. The amount authorized is $30,000 in 1997, $770,000 in 1998 and $760,000 in 1999. Total development costs incurred and charged to the plan in 1998 amounted to $627,000 (1997: $nil).

Note 17 Budget Information

The accrued benefits are based on the Local Authorities Pension Plan Board of Trustees' best estimates of future events after consultation with the plan's actuary. Differences between actual results and the board's expectations are disclosed as experience gains and losses in the statement of changes in accrued benefits. Accordingly, a budget is not included in these financial statements.

Note 18 Uncertainty Due to the Year 2000

The year 2000 issue is the result of some computer systems using two digits rather than four to define the applicable year. Computer systems that have date sensitive software may recognize a date using "00" as the year 1900 rather than the year 2000, which could result in miscalculations or system failures. In addition, similar problems may arise in some systems if certain dates in 1999 are not recognized as a valid date or are recognized to represent something other than a date. The effects of the year 2000 issue may be experienced before, on, or after January 1, 2000. If not addressed, the effect on operations and financial reporting may range from minor errors to significant systems failure that could affect the ability to conduct some operations. Despite efforts to address this issue, it is not possible to be certain that all aspects of the year 2000 issue affecting the plan, including those related to the efforts of customers, suppliers and other third parties, will be fully resolved.

Note 19 Comparative Figures

Comparative figures have been restated to be consistent with the 1998 presentation.

Note 20 Approval of Financial Statements

These financial statements were approved by the Local Authorities Pension Plan Board of Trustees.

# LOCAL AUTHORITIES PENSION PLAN
## SCHEDULE OF INVESTMENTS IN CANADIAN DOLLAR PUBLIC BOND POOL (a)(b)
## DECEMBER 31, 1998
($ thousands)

| | 1998 | | 1997 | |
|---|---|---|---|---|
| | Plan's Share | Total Pool | Plan's Share | Total Pool |
| Deposit in the Consolidated | | | | |
| Cash Investment Trust Fund | $ 16,476 | $ 46,902 | $ 35,102 | $ 95,277 |
| Public Fixed Income Securities | | | | |
| Government of Canada, | | | | |
| direct and guaranteed | 939,239 | 2,673,774 | 1,014,505 | 2,753,641 |
| Provincial: | | | | |
| Alberta, direct and guaranteed | 68,763 | 195,750 | 95,599 | 259,481 |
| Other, direct and guaranteed | 406,638 | 1,157,596 | 406,405 | 1,103,095 |
| Municipal | 22,575 | 64,266 | 32,098 | 87,124 |
| Corporate | 1,022,736 | 2,911,470 | 966,719 | 2,623,937 |
| Private Fixed Income Securities | | | | |
| Corporate | 399,604 | 1,137,571 | - | - |
| Total deposit and fixed-income securities | 2,876,031 | 8,187,329 | 2,550,428 | 6,922,555 |
| Receivable from sale of investments | | | | |
| and accrued investment income | 39,053 | 111,173 | 32,205 | 87,414 |
| Liabilities for investment purchases | (11,712) | (33,341) | (5,477) | (14,868) |
| | 27,341 | 77,832 | 26,728 | 72,546 |
| | $ 2,903,372 | $ 8,265,161 | $ 2,577,156 | $ 6,995,101 |

(a) The Canadian Dollar Public Bond Pool is managed with the objective of providing competitive returns comparable to the total return of the Scotia Capital Markets Universe Bond Index over a four-year period while maintaining adequate security and liquidity of participants' capital. The portfolio is comprised of high quality Canadian fixed income instruments and debt-related derivatives. Competitive returns are achieved through management of the portfolio duration and sector rotation.

(b) Fixed income securities had an average effective current yield of 5.44% per annum based on market value (1997: 5.53% per annum). The following term structure of these securities as at December 31 is based on par value.

| | 1998 | 1997 |
|---|---|---|
| | % | |
| under 1 year | 11 | 6 |
| 1 to 5 years | 36 | 40 |
| 5 to 10 years | 26 | 23 |
| 10 to 20 years | 18 | 16 |
| over 20 years | 9 | 15 |
| | 100 | 100 |

# LOCAL AUTHORITIES PENSION PLAN
## SCHEDULE OF INVESTMENTS IN CANADIAN POOLED EQUITIES FUND (a)
## DECEMBER 31, 1998

($ thousands)

| | 1998 | | 1997 | |
|---|---|---|---|---|
| | Plan's Share | Total Pool | Plan's Share | Total Pool |
| Deposit in the Consolidated Cash Investment Trust Fund | $ 3,605 | $ 7,321 | $ 72,095 | $ 141,051 |
| Canadian Public Equities (b) | | | | |
| Common shares and rights: | | | | |
| Communications and media | 31,576 | 64,115 | 56,044 | 109,648 |
| Conglomerates | 41,438 | 84,138 | 86,582 | 169,396 |
| Consumer products | 60,092 | 122,014 | 66,560 | 130,222 |
| Financial services | 201,562 | 409,265 | 385,794 | 754,796 |
| Gold and precious minerals | 39,794 | 80,800 | 69,159 | 135,308 |
| Industrial products | 158,754 | 322,345 | 309,769 | 606,054 |
| Merchandising | 19,302 | 39,192 | 57,353 | 112,209 |
| Metals and minerals | 35,034 | 71,135 | 96,692 | 189,175 |
| Oil and gas | 72,950 | 148,122 | 300,294 | 587,518 |
| Paper and forest products | 18,832 | 38,238 | 53,752 | 105,164 |
| Pipelines | 24,609 | 49,968 | 39,856 | 77,978 |
| Real estate and construction | 20,445 | 41,512 | 31,523 | 61,673 |
| Transportation and environmental services | 30,534 | 61,998 | 80,884 | 158,248 |
| Utilities | 102,157 | 207,427 | 155,483 | 304,198 |
| | 857,079 | 1,740,269 | 1,789,745 | 3,501,587 |
| Passive index | 4,266 | 8,663 | 7,304 | 14,291 |
| Options and other | - | - | 581 | 1,137 |
| | 861,345 | 1,748,932 | 1,797,630 | 3,517,015 |
| Receivable from sale of investments and accrued investment income | 11,837 | 24,034 | 9,411 | 18,413 |
| Liabilities for investment purchases | (8,695) | (17,657) | (4,367) | (8,544) |
| | 3,142 | 6,377 | 5,044 | 9,869 |
| | $ 868,092 | $ 1,762,630 | $ 1,874,769 | $ 3,667,935 |

(a) The Canadian Pooled Equities Fund (CPE) is managed with the objective of providing returns higher than the total return of the Toronto Stock Exchange 300 Index over a four-year period while maintaining preservation of participants' capital. The portfolio is comprised of publicly traded equities in Canadian corporations. Risk is reduced by prudent security selection and sector rotation. During the year, a portion of the plan's investments held by the CPE was transferred to the Domestic Passive Equity Pooled Fund through the Transition Account.

(b) The industrial classifications are those used by the Toronto Stock Exchange

# LOCAL AUTHORITIES PENSION PLAN
## SCHEDULE OF INVESTMENTS IN DOMESTIC PASSIVE EQUITY POOLED FUND (a)
## DECEMBER 31, 1998

($ thousands)

| | Plan's Share | Total Pool |
|---|---|---|
| Deposit in the Consolidated Cash Investment Trust Fund | $ 15,512 | $ 34,407 |
| Short-term Securities | 5,826 | 12,924 |
| Floating Rate Note Pool | 262,785 | 582,896 |
| | 284,123 | 630,227 |
| Canadian Public Equities (b): | | |
| Common shares and rights: | | |
| Communications and media | 26,682 | 59,184 |
| Conglomerates | 17,567 | 38,966 |
| Consumer products | 35,735 | 79,267 |
| Financial services | 105,183 | 233,311 |
| Gold and precious minerals | 26,581 | 58,961 |
| Industrial products | 94,811 | 210,306 |
| Merchandising | 19,560 | 43,386 |
| Metals and minerals | 17,044 | 37,807 |
| Oil and gas | 45,647 | 101,252 |
| Paper and forest products | 13,158 | 29,186 |
| Pipelines | 15,275 | 33,881 |
| Real estate and construction | 11,389 | 25,262 |
| Transportation and environmental services | 12,048 | 26,723 |
| Utilities | 61,387 | 136,165 |
| | 502,067 | 1,113,657 |
| Domestic Structured Equity Pooled Fund | 54,703 | 121,340 |
| | 556,770 | 1,234,997 |
| United States Public Equities | 1,143 | 2,535 |
| Receivable from sale of investments and accrued investment income | 16,469 | 36,530 |
| Liabilities for investment purchases | (4,230) | (9,383) |
| | 12,239 | 27,147 |
| | $ 854,275 | $ 1,894,906 |

(a) The Domestic Passive Equity Pooled Fund is managed on a passive approach with the objective of providing investment returns comparable to the Toronto Stock Exchange (TSE) 300 Index. The portfolio is comprised of both publicly traded Canadian equities and structured investments replicating the TSE 100 Index and the TSE 35 Index. A portion of the portfolio fully replicates the TSE 300. The other portion provides investment returns which are comparable to the TSE 100 Index and the TSE 35 Index through directly held swaps or investment in the Domestic Structured Equity Pooled Fund (DSEP). DSEP replicates the TSE 100 Index with index-based securities and structured investments such as index swaps and interest rate swaps. It provides returns comparable to the TSE 100 index. FRNP is managed with the objective of generating floating rate income needed for the swap obligations of the participants with structured investments in equities and bonds. Through the use of structured investments such as interest rate swaps, FRNP provides investment opportunities in high quality floating rate instruments with remaining term-to-maturity of ten years or less.

(b) The industrial classifications are those used by the Toronto Stock Exchange.

# LOCAL AUTHORITIES PENSION PLAN
# SCHEDULE OF INVESTMENTS IN EXTERNAL MANAGERS FUND (a)
# DECEMBER 31, 1998

($ thousands)

| | 1998 | | 1997 | |
|---|---|---|---|---|
| | Plan's Share | Total Pool | Plan's Share | Total Pool |
| Foreign Public Equity Pools | | | | |
| Multi Region | $ 424,384 | $ 1,069,544 | $ 466,845 | $ 1,109,831 |
| Europe | 314,938 | 835,531 | 129,684 | 308,298 |
| Pacific Basin | 175,665 | 457,418 | 157,574 | 374,599 |
| Emerging markets | 18,692 | 47,107 | - | - |
| | 933,679 | 2,409,600 | 754,103 | 1,792,728 |
| United States | 225,552 | 597,487 | 166,140 | 394,964 |
| Canadian Public Equity Pools | | | | |
| Large Cap | 251,202 | 646,679 | - | - |
| Small Cap | 150,653 | 428,952 | 175,297 | 425,762 |
| | 401,855 | 1,075,631 | 175,297 | 425,762 |
| | $ 1,561,086 | $ 4,082,718 | $ 1,095,540 | $ 2,613,454 |

(a) The fund is managed by external managers with expertise in global and Canadian equity markets. The objective of the fund is to provide investment returns higher than the total return of the applicable Morgan Stanley Capital International, Standard & Poor and Toronto Stock Exchange indices over a four-year period. The portfolio is comprised of publicly traded equity securities on Canadian and approved foreign markets. Risk is reduced through manager, style and market diversification.

MANAGEMENT EMPLOYEES PENSION PLAN
FINANCIAL STATEMENTS
DECEMBER 31, 1998



## AUDITOR'S REPORT

To the Provincial Treasurer

I have audited the statement of net assets available for benefits and accrued pension benefits of the Management Employees Pension Plan as at December 31, 1998 and the statements of changes in net assets available for benefits, changes in accrued pension benefits and changes in deficiency for the year then ended. These financial statements are the responsibility of the Plan's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In my opinion, these financial statements present fairly, in all material respects, the financial position of the Plan as at December 31, 1998 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles.

Peter Valentine, FCA
Auditor General

Edmonton, Alberta
April 19, 1999

# MANAGEMENT EMPLOYEES PENSION PLAN
## STATEMENT OF NET ASSETS AVAILABLE FOR BENEFITS AND ACCRUED BENEFITS AS AT DECEMBER 31, 1998

($ thousands)

| | 1998 | 1997 |
|---|---|---|
| **Net Assets Available for Benefits** | | |
| Assets | | |
| Investments (Note 3) | $ 1,305,852 | $ 1,197,866 |
| Accrued investment income | 213 | 396 |
| Contributions receivable (Note 6) | 3,112 | 2,579 |
| | 1,309,177 | 1,200,841 |
| Liabilities | | |
| Accounts payable (Note 7) | 469 | 178 |
| Net assets available for benefits | 1,308,708 | 1,200,663 |
| Actuarial asset fluctuation reserve [Note 2(c)] | (15,800) | (41,500) |
| Actuarial value of net assets available for benefits | 1,292,908 | 1,159,163 |
| **Accrued Benefits** | | |
| Actuarial value of accrued benefits | 1,250,853 | 1,165,653 |
| Actuarial surplus (deficiency) (Note 10) | $ 42,055 | $ (6,490) |

*See accompanying notes and schedules.*

# MANAGEMENT EMPLOYEES PENSION PLAN
## STATEMENT OF CHANGES IN NET ASSETS AVAILABLE FOR BENEFITS FOR THE YEAR ENDED DECEMBER 31, 1998

($ thousands)

| | 1998 | 1997 |
|---|---|---|
| Increase in assets | | |
| Investment income (Note 8) | $ 105,296 | $ 132,257 |
| Contributions | | |
| Current and past service | | |
| Employers | 17,000 | 15,321 |
| Employees | 15,175 | 14,116 |
| Unfunded liability | | |
| Employers | 5,762 | 5,267 |
| Employees | 1,571 | 1,436 |
| Transfers from other plans | 34 | 24 |
| | 39,542 | 36,164 |
| Total increase in assets | 144,838 | 168,421 |
| Decrease in assets | | |
| Pension benefits | 33,483 | 27,820 |
| Refunds to members | 2,651 | 2,680 |
| Transfers to other plans | - | 83 |
| Administration expenses (Note 9) | 659 | 578 |
| Total decrease in assets | 36,793 | 31,161 |
| Increase in net assets for the year | 108,045 | 137,260 |
| Net assets available for benefits at beginning of year | 1,200,663 | 1,063,403 |
| Net assets available for benefits at end of year | $ 1,308,708 | $ 1,200,663 |

*See accompanying notes and schedules.*

## MANAGEMENT EMPLOYEES PENSION PLAN
## STATEMENT OF CHANGES IN ACCRUED BENEFITS
## FOR THE YEAR ENDED DECEMBER 31, 1998

($ thousands)

| | 1998 | | | 1997 |
|---|---|---|---|---|
| | Pre-1992 | Post 1991 | Total | Total |
| Increase in accrued benefits | | | | |
| Interest accrued on benefits | $ 68,400 | $ 21,600 | $ 90,000 | $ 80,500 |
| Benefits earned | - | 32,200 | 32,200 | 32,800 |
| Net experience losses | - | - | - | 11,400 |
| Increase in accrued benefits | 68,400 | 53,800 | 122,200 | 124,700 |
| Decrease in accrued benefits | | | | |
| Net benefits paid | 31,100 | 5,900 | 37,000 | 24,900 |
| Decrease in accrued benefits | 31,100 | 5,900 | 37,000 | 24,900 |
| Net increase in accrued benefits | 37,300 | 47,900 | 85,200 | 99,800 |
| Accrued benefits at beginning of year | 910,171 | 255,482 | 1,165,653 | 1,065,853 |
| Accrued benefits at end of year (Note 10) | $ 947,471 | $ 303,382 | $ 1,250,853 | $ 1,165,653 |

*See accompanying notes and schedules*

## MANAGEMENT EMPLOYEES PENSION PLAN
## STATEMENT OF CHANGES IN ACTUARIAL SURPLUS
## FOR THE YEAR ENDED DECEMBER 31, 1998

($ thousands)

| | 1998 | | | 1997 |
|---|---|---|---|---|
| | Pre-1992 | Post-1991 | Total | Total |
| Actuarial surplus (deficiency) at beginning of year | $ (26,708) | $ 20,218 | $ (6,490) | $ (86,550) |
| Net increase in net assets available for benefits | 56,637 | 51,408 | 108,045 | 137,260 |
| Net decrease in actuarial asset fluctuation reserve | 20,700 | 5,000 | 25,700 | 42,600 |
| Net increase in accrued benefits | (37,300) | (47,900) | (85,200) | (99,800) |
| Actuarial surplus (deficiency) at end of year | $ 13,329 | $ 28,726 | $ 42,055 | $ (6,490) |

*See accompanying notes and schedules.*

MANAGEMENT EMPLOYEES PENSION PLAN
NOTES TO THE FINANCIAL STATEMENTS
DECEMBER 31, 1998

Note 1 Summary Description of the Plan

The following description of the Management Employees Pension Plan is a summary only. For a complete description of the plan, reference should be made to the *Public Sector Pension Plans Act*, Chapter P-30.7, Statutes of Alberta 1993 and Alberta Regulation 367/93.

(a) General

The Management Employees Pension Plan is a contributory defined benefit pension plan for eligible management employees of the Province of Alberta and certain approved provincial agencies and public bodies. Members of the former Public Service Management Pension Plan who were active contributors at August 1, 1992 continue as members of this plan.

(b) Funding

Current service costs are funded by employer and employee contributions at rates which are expected to provide for all benefits payable under the plan. The rates in effect at December 31, 1998 are 8.0% of pensionable salary for employers and 7.0% for employees. The rates are to be reviewed at least once every three years by Alberta Treasury based on recommendations of the plan's actuary.

The unfunded liability for service prior to January 1, 1992 as determined by actuarial valuation is financed by additional contributions from employers and employees. The rates are set so that additional contributions will eliminate the unfunded liability on or before December 31, 2043. Transitional rates based on the pensionable salary are 2.75% for employers and 0.75% for employees.

(c) Retirement Benefits

The plan provides a pension of 2.0% for each year of pensionable service based on the average salary of the highest five consecutive years. The maximum service allowable under the plan is 35 years.

Members are entitled to an unreduced pension on service before 1992 if they have attained age 55 and have at least five years of service.

Members are entitled to an unreduced pension on service after 1991 if they retire with at least five years of service and have either attained age 60 or age 55 and the sum of their age and service equals 80. Pensions on service after 1991 are reduced if the member is under age 60 and the 80 factor is not attained.

(d) Disability Benefits

Pensions are payable to members who become totally disabled and retire early with at least five years of service. Reduced pensions are payable to members who become partially disabled and retire early with at least five years of service.

(e) Death Benefits

Death benefits are payable on the death of a member. If the member has at least five years of service, a surviving spouse may choose to receive a survivor pension. For a beneficiary other than a spouse, or where service is less than five years, a lump sum payment must be chosen.

(f) Termination Benefits

Members who terminate with fewer than five years of service receive a refund of their own contributions plus interest.

Members who terminate with more than five years of service and are not immediately entitled to a pension may apply for a refund or a deferred pension. A refund is based on contributions and interest in relation to service before 1992 and commuted value for service after 1991. Refunds are subject to the plan's lock-in provisions.

(g) Guarantee

The Province of Alberta guarantees payment of all benefits arising from service before 1994.

(h) Prior Service and Transfers

All prior service purchases are to be cost-neutral to the plan.

All existing reciprocal agreements were terminated in 1994. New reciprocal agreements were or are being renegotiated to provide that transferred-in service be on an actuarial reserve basis and transfers out receive the greater of the termination benefits or commuted value for all service.

(i) Cost-of-Living Adjustments

Pensions payable are increased each year by an amount equal to at least 60% of the increase in the Alberta Consumer Price Index.

(j) Income Taxes

The plan is a registered pension plan as defined in the *Income Tax Act*. The plan's registration number is 0570887.

Note 2 Summary of Significant Accounting Policies and Reporting Practices

(a) Basis of Presentation

These financial statements are prepared on the going concern basis in accordance with generally accepted accounting principles. The statements provide information about the net assets available in the plan to meet future benefit payments and are prepared to assist plan members and others in reviewing the activities of the plan for the year. They do not reflect the funding requirements of the plan or the benefit security of individual participants.

The majority of plan investments are held in pooled investment funds administered by Alberta Treasury. Pooled investment funds have a market-based unit value that is used to allocate income to participants and to value purchases and sales of pool units.

The plan's respective percentage ownership in pooled investment funds at December 31 was as follows:

| | % Ownership | |
|---|---|---|
| | 1998 | 1997 |
| Canadian Dollar Public Bond Pool | 6.2 | 6.6 |
| Canadian Pooled Equities Fund | 8.4 | 8.6 |
| Domestic Passive Equity Pooled Fund | 7.6 | - |
| External Managers Fund | 6.2 | 6.7 |
| Global Structured Equity Pooled Fund | 6.0 | 6.0 |
| Private Bond Pool | 6.9 | 7.9 |
| Private Equity Pool | 7.8 | 8.2 |
| Private Mortgage Pool | 6.7 | 5.9 |
| Private Real Estate Pool | 5.3 | 6.1 |
| Transition Account | 9.9 | - |
| United States Pooled Equities Fund | 6.3 | 6.7 |
| US Passive Equity Pooled Fund | 6.3 | - |

(b) Valuation of Assets and Liabilities

Investments are stated at fair value. The methods used to determine the fair value of investments held either by the plan or by pooled investment funds are explained in the following paragraphs.

Short-term securities, public fixed income securities and equities are valued at the year-end closing sale price or the average of the latest bid and ask prices quoted by an independent securities valuation company.

Private fixed income securities and mortgages are valued based on the net present value of future cash flows. These cash flows are discounted using Government of Canada bond rates adjusted for a risk premium estimated by management.

The fair value of private equities is estimated by management.

Real estate investments are reported at their most recent appraised value net of any liabilities against the real property. Real estate properties are appraised annually by qualified external real estate appraisers.

The fair values of deposits, receivables, accrued investment income and payables are estimated to approximate their book values.

(c) Actuarial Value of Net Assets Available for Benefits

To moderate the effects of market volatility on investment value, annual net unrealized gains and losses are amortized equally over three years.

(d) Income Recognition

Dividends are accrued on the ex-dividend date. Income from other investments is accrued as earned. Gains or losses on investments are recognized concurrently with changes in fair value.

(e) Foreign Exchange

Foreign currency transactions are translated into Canadian dollars using average rates of exchange except for hedged foreign currency transactions, which are translated at rates of exchange established by the terms of the forward exchange contracts. At the year-end the fair value of investments and any other assets and liabilities denominated in a foreign currency are translated at the year-end exchange rate. Exchange differences are included in the determination of investment income.

(f) Derivative Financial Instruments

Income and expense on index swaps and interest rate swaps are accrued as earned and included in investment income. Gains and losses on forward foreign exchange contracts are recognized concurrently with changes in fair value.

Note 3 Investments (Schedules A to D)

Investments are summarized as follows:

| | 1998 | | 1997 | |
|---|---|---|---|---|
| | ($ thousands) | % | ($ thousands) | % |
| Deposit in the Consolidated Cash | | | | |
| Investment Trust Fund (a) | $ 4,043 | 0.3 | $ 12,449 | 1.0 |
| Fixed Income Securities | | | | |
| Canadian Dollar Public Bond Pool (Schedule A) | 515,657 | 39.5 | 463,197 | 38.7 |
| Private Mortgage Pool (b) | 61,645 | 4.7 | 46,540 | 3.9 |
| Real Rate of Return Bonds (c) | 20,191 | 1.6 | 19,753 | 1.7 |
| Private Bond Pool | 112 | - | 33,736 | 2.8 |
| Total deposit and fixed income securities | 601,648 | 46.1 | 575,675 | 48.1 |
| Canadian Equities | | | | |
| Canadian Pooled Equities Fund (Schedule B) | 147,560 | 11.3 | 316,413 | 26.4 |
| Transition Account and miscellaneous | 114 | - | - | - |
| Domestic Passive Equity Pooled Fund (Schedule C) | 144,180 | 11.0 | - | - |
| External Managers Fund (Canadian) (Schedule D) | 65,728 | 5.0 | 28,588 | 2.4 |
| Private Equity Pool (d) | 7,450 | 0.6 | 9,950 | 0.8 |
| | 365,032 | 27.9 | 354,951 | 29.6 |
| Foreign Equities | | | | |
| External Managers Fund (Global) (Schedule D) | 151,672 | 11.6 | 119,592 | 10.0 |
| Global Structured Equity Pooled Fund (e) | 81,187 | 6.2 | 49,948 | 4.2 |
| US Passive Equity Pooled Fund (f) | 38,068 | 2.9 | - | - |
| External Managers Fund (United States) (Schedule D) | 37,609 | 2.9 | 26,348 | 2.2 |
| United States Pooled Equities Fund | 1,007 | 0.1 | 43,463 | 3.6 |
| | 309,543 | 23.7 | 239,351 | 20.0 |
| Equities in Real Estate | | | | |
| Private Real Estate Pool (g) | 29,629 | 2.3 | 27,889 | 2.3 |
| Total equities | 704,204 | 53.9 | 622,191 | 51.9 |
| Total investments | $1,305,852 | 100.0 | $1,197,866 | 100.0 |

(a) The Consolidated Cash Investment Trust Fund is managed with the objectives of providing competitive interest income to depositors while maintaining maximum security and liquidity of depositors' capital. The portfolio is comprised of high-quality short-term and mid-term fixed income securities with a maximum term to maturity of five years.

(b) The Private Mortgage Pool is managed with the objective of providing investment returns higher than attainable from the publicly traded bond market over the long term. The portfolio is comprised primarily of high-quality commercial mortgage loans. In order to reduce risk, the pool only invests in loans insured by a federal agency and first-mortgage loans that provide diversification by property usage. The pool does not invest in mortgages on single family houses, hotels, motels, trailer parks or recreational properties. As at December 31, 1998, mortgages held by the pool have an average effective yield of 6.92% per annum based on market (1997: 7.64%). Approximately 90% of the mortgages held will mature within ten years (1997: 91%).

(c) Bonds are issued or guaranteed by the Government of Canada, bear interest at a fixed rate adjusted for inflation, and have terms to maturity of over 20 years.

(d) The Private Equity Pool is managed with the objective of providing investment returns higher than attainable from publicly traded equity indices such as the Toronto Stock Exchange 300 Index over the long term. The portfolio is comprised of equity investments in companies that show higher than average growth potential. Risk is reduced by avoiding direct investments in start-up and venture capital situations and by limiting holdings in any single company.

(e) The Global Structured Equity Pooled Fund is managed with the objective of providing investment returns comparable to the total return of the Morgan Stanley Capital International World Index. The pooled fund provides exposure to global markets through the use of structured investments such as foreign equity index swaps and interest rate swaps. All payments and receipts relating to swaps are in Canadian dollars. Participation in the pooled fund qualifies as a Canadian investment under the *Income Tax Act*.

(f) The US Passive Equity Pooled Fund is managed with the objective of attaining investment returns comparable to Standard & Poor's (S & P) 500 Total Return Index over a four-year period. The portfolio is comprised of publicly traded equities in the United States similar in weights to the S & P 500 Index. To enhance investment returns with no substantial increase in risks, the pooled fund also invests in futures, swaps and other structured investments.

(g) The Private Real Estate Pool is managed with the objective of providing investment returns comparable to the Russell Canadian Property Index over the long term. Real estate is held through intermediate companies, which have issued to the pool common shares and participating debentures secured by a charge on real estate. Risk is reduced by investing in properties that provide diversification by geographic location, by property type and by tenancy. The plan's investments in the pool were sold for $29.6 million in January 1999.

## Note 4 Investment Risk Management

Actuarial liabilities of the plan are primarily affected by the long-term real rate of return on investments. Fair values of investments are exposed to credit risk and price risk. Credit risk relates to the possibility that a loss may occur from the failure of another party to perform according to the terms of a contract. Price risk is comprised of currency risk, interest rate risk and market risk. Currency risk relates to the possibility that the investments will change in value due to future fluctuations in foreign exchange rates. Interest rate risk relates to the possibility that the investments will change in value due to future fluctuations in market interest rates. Market risk relates to the possibility that the investments will change in value due to future fluctuations in market prices.

In order to earn the best possible return at an acceptable level of risk, the board has established a policy asset mix of 40% to 60% fixed income instruments and 40% to 60% equities. Risk is reduced through asset class diversification, diversification within each asset class, quality constraints on fixed income instruments, and restrictions on amounts exposed to countries designated as emerging markets. Borrowing or leveraging is not allowed with the exception of pre-existing mortgages on real estate properties. Controls are in place respecting the use of derivatives (see Note 5). Forward foreign exchange contracts are used to manage currency exposure in connection with securities purchased in foreign currency (see Note 5).

## Note 5 Index Swaps, Interest Rate Swaps and Foreign Exchange Contracts

Pooled funds use index and interest rate swaps to enhance return and for hedging risks. A swap is a contractual agreement between two parties to exchange a series of cash flows based on a notional amount and does not involve the exchange of the underlying principal. An index swap involves the exchange of a floating interest rate cash flow for one based on the performance of a market index. For interest rate swaps, parties generally exchange fixed and floating rate interest cash flows based on a notional value. There are underlying securities supporting all swaps. Leveraging is not allowed.

The following is a summary of the plan's proportionate share of the notional value of index and interest rate swaps held or issued by pooled funds at December 31, 1998.

| | 1998 | 1997 |
|---|---|---|
| | ($ thousands) | |
| Index swaps | | |
| Foreign equities | | |
| Global Structured Equity Pooled Fund | $ 75,766 | $ 39,332 |
| US Passive Equity Pooled Fund | 38,081 | - |
| Canadian equities - Domestic Passive Equity Pooled Fund | 58,534 | - |
| Bonds - Canadian Dollar Public Bond Pool | 94,390 | 63,770 |
| Interest rate swaps | | |
| Fixed to floating | | |
| Canadian Dollar Public Bond Pool | 63,255 | 26,196 |
| Domestic Passive Equity Pooled Fund | 39,939 | - |
| Global Structured Equity Pooled Fund | 50,654 | 33,541 |
| US Passive Equity Pooled Fund | 3,545 | - |
| | $ 424,164 | $ 162,839 |

Foreign exchange contracts are contractual agreements to exchange specified currencies at an agreed upon exchange rate and on an agreed settlement date in the future. As at December 31, 1998, the plan's proportionate share of outstanding forward foreign exchange contracts issued by the External Managers Fund amounted to $29,204,000 (1997: $24,603,000).

Note 6 Contributions Receivable

| | 1998 | 1997 |
|---|---|---|
| | ($ thousands) | |
| Employers | $ 1,803 | $ 1,473 |
| Employees | 1,309 | 1,106 |
| | $ 3,112 | $ 2,579 |

Note 7 Accounts Payable

| | 1998 | 1997 |
|---|---|---|
| | ($ thousands) | |
| Benefits | $ 16 | $ 15 |
| Refunds and transfers | 320 | 90 |
| Administration expenses | 133 | 73 |
| | $ 469 | $ 178 |

Note 8 Investment Income

| | 1998 | | | 1997 |
|---|---|---|---|---|
| | Income (a) | Change in Fair Value | Total | Total |
| | ($ thousands) | | | |
| Deposits and Fixed Income Securities: | | | | |
| Deposit in the Consolidated Cash Investment Trust Fund | $ 646 | $ - | $ 646 | $ 1,013 |
| Canadian Dollar Public Bond Pool | 30,978 | 10,434 | 41,412 | 39,387 |
| Private Mortgage Pool | 4,887 | 654 | 5,541 | 3,480 |
| Real Rate of Return Bonds | 999 | 516 | 1,515 | 885 |
| Private Bond Pool | 2,883 | - | 2,883 | 1,289 |
| | 40,393 | 11,604 | 51,997 | 46,054 |
| Equities: | | | | |
| Canadian Pooled Equities Fund | 3,798 | (9,211) | (5,413) | 40,927 |
| Transition Account and miscellaneous | 2,831 | 15,097 | 17,928 | - |
| Domestic Passive Equity Pooled Fund | (4,675) | (17,663) | (22,338) | - |
| External Managers Fund (Canadian) | 387 | (582) | (195) | 5,273 |
| Private Equity Pool | 139 | (213) | (74) | 728 |
| External Managers Fund (Global) | 2,068 | 29,542 | 31,610 | 6,651 |
| Global Structured Equity Pooled Fund | 11,271 | (31) | 11,240 | 8,975 |
| US Passive Equity Pooled Fund | 5,878 | 2,258 | 8,136 | - |
| External Managers Fund (United States) | 225 | 10,367 | 10,592 | 7,930 |
| United States Pooled Equities Fund | 2 | (1,640) | (1,638) | 10,958 |
| Private Real Estate Pool | 1,391 | 2,060 | 3,451 | 4,761 |
| | 23,315 | 29,984 | 53,299 | 86,203 |
| | $ 63,708 | $ 41,588 | $ 105,296 | $ 132,257 |

(a) Income is comprised of dividends, interest and rental income.

Note 9 Administration Expenses

| | 1998 | 1997 |
|---|---|---|
| | ($ thousands) | |
| General administration costs | $ 438 | $ 370 |
| Investment management costs | 219 | 164 |
| Actuarial fees | 2 | 44 |
| | $ 659 | $ 578 |

General administration costs including board costs were paid to Alberta Pensions Administration Corporation on a cost-recovery basis.

Investment management costs were paid to Alberta Treasury and do not include custodial and external management fees, which have been deducted in arriving at investment income.

In 1998, total administration costs of $659,000 amounted to $124 per member (1997: $114 per member). The $10 per member cost increase in 1998 is attributed to the following factors: changes in the accounting treatment of business process reengineering cost $12, increase in investment management cost $9, and decrease in plan specific cost ($11).

Note 10 Accrued Benefits

(a) Actuarial Valuation

An actuarial valuation of the plan was carried out as at December 31, 1997 by William M. Mercer Limited and was then extrapolated to December 31, 1998. The December 31, 1997 valuation resulted in an actuarial deficiency of $6.5 million as disclosed in the statement of net assets available for benefits and accrued benefits.

The valuation was determined as at December 31, 1997 using the projected benefit method prorated on service. The assumptions used in the valuation were developed as the best estimate of expected short-term and long-term market conditions and other future events. This estimate was, after consultation with the plan's actuary, approved by the Management Employees Pension Board.

The major assumptions used were:

| | December 31 | |
|---|---|---|
| | 1998 Extrapolation % | 1997 Valuation % |
| Asset real rate of return | 4.0 | 4.0 |
| Inflation rate (after phasing-in) | 3.5 | 3.5 |
| Investment rate of return | 7.5 | 7.5 |
| Salary escalation rate (after phasing-in) | | |
| Disclosed rate plus merit and promotion | 3.5 | 3.5 |
| Pension cost-of-living increase as a percentage of Alberta Consumer Price Index | 60.0 | 60.0 |

In accordance with the requirements of the *Public Sector Pension Plans Act*, a separate accounting is required of the pension liability with respect to service recognized as pensionable as at December 31, 1991. The following table summarizes the accrued benefits, actuarial value of net assets and the resulting actuarial surplus or deficiency at December 31, 1998:

| | 1998 | | | 1997 |
|---|---|---|---|---|
| | Pre-1992 | Post-1991 | Total | Total |
| | ($ thousands) | | | |
| Fair value of net assets | $ 972,800 | $ 335,908 | $ 1,308,708 | $ 1,200,663 |
| Actuarial asset fluctuation reserve | (12,000) | (3,800) | (15,800) | (41,500) |
| Actuarial value of net assets | 960,800 | 332,108 | 1,292,908 | 1,159,163 |
| Accrued pension benefits | 947,471 | 303,382 | 1,250,853 | 1,165,653 |
| Actuarial surplus | $ 13,329 | $ 28,726 | $ 42,055 | $ (6,490) |

(b) Sensitivity of Changes in Major Assumptions

The plan's future experience will inevitably differ, perhaps significantly, from the assumptions used in the actuarial valuation. Any differences between the actuarial assumptions and future experience will emerge as gains or losses in future valuations and will affect the financial position of the plan.

As at December 31, 1998, holding the nominal investment return and salary escalation assumptions constant, a 1% increase in the assumed long-term inflation rate would result in actuarial surplus of the plan changing from a surplus of $42.1 million to a deficiency of $55.8 million.

As at December 31, 1998 holding the inflation and nominal investment return assumptions constant, a 1% increase in the assumed salary escalation would result in the actuarial surplus of the plan decreasing from $42.1 million to $10.1 million.

As at December 31, 1998, holding the inflation rate and salary escalation assumptions constant, a 1% decrease in the assumed long-term investment return would result in a change in the actuarial surplus of the plan from $42.1 million to a deficiency of $163.7 million.

Note 11 Budget Information

The accrued benefits are based on the Management Employees Pension Board's best estimates of future events. Differences between actual results and the board's expectations are disclosed as net experience gains and losses in the statement of changes in accrued benefits. Accordingly, a budget is not included in these financial statements.

Note 12 Uncertainty Due to the Year 2000

The year 2000 issue is the result of some computer programs being written using two digits rather than four to define the applicable year. Computer programs that have date sensitive software may recognize a date using "00" as the year 1900 rather than the year 2000, which could result in miscalculations or system failures. In addition, similar problems may arise in some systems if certain dates in 1999 are not recognized as a valid date or are recognized to represent something other than a date. The effects of the year 2000 issue may be experienced before, on, or after January 1, 2000. If not addressed, the effect on operations and financial reporting may range from minor errors to significant systems failure that could affect the ability to conduct some operations. Despite efforts to address this issue, it is not possible to be certain that all aspects of the year 2000 issue affecting the plan, including those related to the efforts of suppliers and other third parties, will be fully resolved.

Note 13 Subsequent Event

Subsequent to the year-end, the board has authorized an actuarial valuation of the plan to be carried out as at December 31, 1998 to facilitate the withdrawal of all active members of Alberta Treasury Branches from the plan effective January 1, 1999. Any differences between the actuarial valuation results and extrapolation results as reported in these financial statements will affect the financial position of the plan and will be accounted for as gains or losses in 1999.

Note 14 Comparative Figures

Comparative figures have been restated to be consistent with the 1998 presentation.

Note 15 Responsibility for Financial Statements

These financial statements were prepared by management and approved by the Management Employees Pension Board.

Schedule A

# MANAGEMENT EMPLOYEES PENSION PLAN
## SCHEDULE OF INVESTMENTS IN CANADIAN DOLLAR PUBLIC BOND POOL (a) (b)
## AS AT DECEMBER 31, 1998
($ thousands)

| | Plan's Share | |
|---|---|---|
| | 1998 | 1997 |
| Deposit in the Consolidated Cash Investment Trust Fund | $ 2,926 | $ 6,309 |
| Public Fixed Income Securities | | |
| Government of Canada, direct and guaranteed | 166,815 | 182,339 |
| Provincial: | | |
| Alberta, direct and guaranteed | 12,213 | 17,182 |
| Other, direct and guaranteed | 72,221 | 73,044 |
| Municipal | 4,009 | 5,769 |
| Corporate | 181,645 | 173,750 |
| Private Fixed Income Securities | | |
| Corporate | 70,972 | - |
| Total deposit and fixed income securities | 510,801 | 458,393 |
| Receivable from sale of investments and accrued investment income | 6,936 | 5,788 |
| Liabilities for investment purchases | (2,080) | (984) |
| | 4,856 | 4,804 |
| | $ 515,657 | $ 463,197 |

(a) The Canadian Dollar Public Bond Pool is managed with the objective of providing competitive returns comparable to the total return of the Scotia Capital Markets Universe Bond Index over a four-year period while maintaining adequate security and liquidity of participants' capital. The portfolio is comprised of high quality Canadian fixed income instruments and related derivatives. Competitive returns are achieved through management of the portfolio duration and sector rotation.

(b) Fixed income securities had an average effective current yield of 5.44% per annum based on market value (1997: 5.53% per annum). The following term structure of these securities as at December 31, 1998 is based on par value.

| | 1998 | 1997 |
|---|---|---|
| | % | |
| under 1 year | 11 | 6 |
| 1 to 5 years | 36 | 40 |
| 5 to 10 years | 26 | 23 |
| 10 to 20 years | 18 | 16 |
| over 20 years | 9 | 15 |
| | 100 | 100 |

Schedule B

# MANAGEMENT EMPLOYEES PENSION PLAN
## SCHEDULE OF INVESTMENTS IN CANADIAN POOLED EQUITIES FUND (a)
## AS AT DECEMBER 31, 1998

($ thousands)

| | Plan's Share | |
|---|---|---|
| | 1998 | 1997 |
| Deposit in the Consolidated Cash Investment Trust Fund | $ 613 | $ 12,168 |
| Canadian Public Equities (b) : | | |
| Common shares and rights: | | |
| Communications and media | 5,368 | 9,459 |
| Conglomerates | 7,044 | 14,613 |
| Consumer products | 10,215 | 11,234 |
| Financial services | 34,262 | 65,112 |
| Gold and precious minerals | 6,764 | 11,672 |
| Industrial products | 26,985 | 52,280 |
| Merchandising | 3,281 | 9,680 |
| Metals and minerals | 5,955 | 16,319 |
| Oil and gas | 12,400 | 50,682 |
| Paper and forest products | 3,201 | 9,072 |
| Pipelines | 4,183 | 6,727 |
| Real estate and construction | 3,475 | 5,320 |
| Transportation and environmental services | 5,190 | 13,651 |
| Utilities | 17,365 | 26,242 |
| | 145,688 | 302,063 |
| Passive index | 725 | 1,233 |
| Options and other | - | 98 |
| | 146,413 | 303,394 |
| Receivable from sale of investments and accrued investment income | 2,012 | 1,588 |
| Liabilities for investment purchases | (1,478) | (737) |
| | 534 | 851 |
| | $ 147,560 | $ 316,413 |

(a) The Canadian Pooled Equities Fund (CPE) is managed with the objective of providing returns higher than the total return of the Toronto Stock Exchange 300 Index over a four-year period while maintaining preservation of participants' capital. The portfolio is comprised of publicly traded equities in Canadian corporations. Risk is reduced by prudent security selection and sector rotation. During the year, a portion of the plan's investments held by the CPE was transferred to the Domestic Passive Equity Pooled Fund through the Transition Account

(b) The industrial classifications are those used by the Toronto Stock Exchange.

Schedule C

# MANAGEMENT EMPLOYEES PENSION PLAN
## SCHEDULE OF INVESTMENTS IN DOMESTIC PASSIVE EQUITY POOLED FUND (a)
## AS AT DECEMBER 31, 1998

($ thousands)

| | Plan's Share |
|---|---|
| Deposit in the Consolidated Cash Investment Trust Fund | $ 2,618 |
| Short-term Securities | 983 |
| Floating Rate Note Pool | 44,351 |
| | 47,952 |
| Canadian Public Equities (b) : | |
| Common shares and rights: | |
| Communications and media | 4,503 |
| Conglomerates | 2,965 |
| Consumer products | 6,031 |
| Financial services | 17,752 |
| Gold and precious minerals | 4,486 |
| Industrial products | 16,002 |
| Merchandising | 3,301 |
| Metals and minerals | 2,877 |
| Oil and gas | 7,704 |
| Paper and forest products | 2,221 |
| Pipelines | 2,578 |
| Real estate and construction | 1,922 |
| Transportation and environmental services | 2,033 |
| Utilities | 10,361 |
| | 84,736 |
| Domestic Structured Equity Pooled Fund | 9,233 |
| United States Public Equities | 193 |
| Receivable from sale of investments and accrued investment income | 2,780 |
| Liabilities for investment purchases | (714) |
| | 2,066 |
| | $ 144,180 |

(a) The Domestic Passive Equity Pooled Fund is managed on a passive approach with the objective of providing investment returns comparable to the Toronto Stock Exchange (TSE) 300 Index. The portfolio is comprised of publicly traded equities in Canadian corporations similar in weights to the TSE 300 Index. To enhance investment returns with no substantial increase in risks, the pooled fund invests in the Domestic Structured Equity Pooled Fund (DSEP) and the Floating Rate Note Pool (FRNP) which are pooled investment funds administered by Alberta Treasury. DSEP replicates the TSE 100 Index with index-based securities and structured investments such as index swaps and interest rate swaps. It provides returns comparable to the TSE 100 index. FRNP is managed with the objective of providing a reinvestment vehicle for participants with structured investments in equities and bonds. Through the use of structured investments such as interest rate swaps, FRNP provides investment opportunities in high quality floating rate instruments with remaining term-to-maturity of ten years or less.

(b) The industrial classifications are those used by the Toronto Stock Exchange.

# MANAGEMENT EMPLOYEES PENSION PLAN
# SCHEDULE OF INVESTMENTS IN EXTERNAL MANAGERS FUND (a)
# AS AT DECEMBER 31, 1998

($ thousands)

| | Plan's Share | |
|---|---|---|
| | 1998 | 1997 |
| Foreign Public Equity Pools | | |
| Multi Region | $ 67,323 | $ 74,036 |
| Europe | 52,592 | 20,567 |
| Pacific Basin | 28,792 | 24,989 |
| Emerging markets | 2,965 | - |
| | 151,672 | 119,592 |
| United States | 37,609 | 26,348 |
| Canadian Public Equity Pools | | |
| Large Cap | 41,159 | - |
| Small Cap | 24,569 | 28,588 |
| | 65,728 | 28,588 |
| | $ 255,009 | $ 174,528 |

(a) The External Managers Fund is managed by external managers with expertise in global and Canadian equity markets. The objective of the fund is to provide investment returns higher than the total return of the applicable Morgan Stanley Capital International, Standard & Poor and Toronto Stock Exchange indices over a four-year period. The portfolio is comprised of publicly traded equity securities on Canadian and approved foreign markets. Risk is reduced through manager, style and market diversification.

PROVINCIAL JUDGES AND MASTERS IN CHAMBERS PENSION PLAN
FINANCIAL STATEMENTS
MARCH 31, 1999



## AUDITOR'S REPORT

To the Provincial Treasurer

I have audited the statement of net assets available for benefits and accrued benefits of the Provincial Judges and Masters in Chambers Pension Plan as at March 31, 1999 and the statement of changes in net assets available for benefits for the year then ended. These financial statements are the responsibility of the Plan's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In my opinion, these financial statements present fairly, in all material respects, the net assets available for benefits and accrued benefits of the Plan as at March 31, 1999 and the results of its operations and the changes in its net assets available for benefits for the year then ended in accordance with generally accepted accounting principles.

Peter Valentine, FCA
Auditor General

Edmonton, Alberta
September 9, 1999

# PROVINCIAL JUDGES AND MASTERS IN CHAMBERS PENSION PLAN
## STATEMENT OF NET ASSETS AVAILABLE FOR BENEFITS AND ACCRUED BENEFITS
## AS AT MARCH 31, 1999

($ thousands)

| | 1999 | 1998 |
|---|---|---|
| **Net Assets Available for Benefits** | | |
| Assets | | |
| Investments (Note 3) | $ 80,940 | $ 78,333 |
| Contributions receivable | 178 | 110 |
| Net assets available for benefits | 81,118 | 78,443 |
| **Accrued Benefits** | | |
| Accrued benefits (Note 6) | 62,262 | 53,717 |
| Actuarial surplus (Note 7) | $ 18,856 | $ 24,726 |

*See accompanying notes and schedules*

# PROVINCIAL JUDGES AND MASTERS IN CHAMBERS PENSION PLAN
## STATEMENT OF CHANGES IN NET ASSETS AVAILABLE FOR BENEFITS
## FOR THE YEAR ENDED MARCH 31, 1999

($ thousands)

| | 1999 | 1998 |
|---|---|---|
| Increase in assets | | |
| Investment income (Note 8) | $ 3,066 | $ 13,056 |
| Contributions | | |
| Current and past service: | | |
| Province of Alberta | 1,244 | 1,319 |
| Provincial Judges and Masters in Chambers | 893 | 5 |
| | 2,137 | 1,324 |
| Total increase in assets | 5,203 | 14,380 |
| Decrease in assets | | |
| Pension benefits | 2,528 | 2,069 |
| Total decrease in assets | 2,528 | 2,069 |
| Increase in net assets for the year | 2,675 | 12,311 |
| Net assets available for benefits at beginning of year | 78,443 | 66,132 |
| Net assets available for benefits at end of year | $ 81,118 | $ 78,443 |

*See accompanying notes and schedules.*

## PROVINCIAL JUDGES AND MASTERS IN CHAMBERS PENSION PLAN
## NOTES TO THE FINANCIAL STATEMENTS
## MARCH 31, 1999

Note 1 Summary Description of the Plan

The following description of the Provincial Judges and Masters in Chambers Pension Plan is a summary only. For a complete description of the plan, reference should be made to the *Provincial Court Judges Act*, Chapter P-20.1, Revised Statutes of Alberta 1980, *Financial Administration Act*, Chapter F-9, Revised Statutes of Alberta 1980 and Alberta Regulation 265/88, as amended.

(a) General

Effective April 1, 1998, the Provincial Judges and Masters in Chambers Pension Plan is a contributory defined benefit pension plan for Provincial Judges and Masters in Chambers of the Province of Alberta.

(b) Funding

Current service costs are funded by the Province of Alberta and plan members at rates which are expected to provide for all benefits payable under the plan. The rates in effect at March 31, 1999 are 9.0% of capped earnings for plan members and 14.05% of capped earnings for the Province. The rates are to be reviewed at least once every three years by the Province based on recommendations of the plan's actuary.

The unfunded liability, if any, as of any particular valuation date is funded by the Province of Alberta on the basis that it is to be liquidated by 20 equal annual contribution payments.

(c) Retirement Benefits

The plan provides for a pension of 2.0% for each year of pensionable service based on the average salary of the highest five consecutive years. Pensionable earnings earned after December 31, 1991 are capped at $86,111 by the *Income Tax Act*. The maximum pensionable service allowable under the plan is 35 years. The normal pensionable age of the plan is 70 years of age.

Members are entitled to an unreduced pension on service before 1992 if they have attained age 55 and have at least five years of service.

Members are entitled to an unreduced pension on service after 1991 if they retire with at least five years of service and have either attained age 60 or age 55 and the sum of their age and service equals 80. Pensions on service after 1991 are reduced if the member is under age 60 and the 80 factor is not attained.

(d) Disability Benefits

Pensions are payable to members who become totally disabled and retire early with at least five years of service. Reduced pensions are payable to members who become partially disabled and retire early with at least five years of service.

(e) Death Benefits

Death benefits are payable on the death of a member. If the member has at least five years of service, a surviving spouse may choose to receive a survivor pension. For a beneficiary other than a spouse or where service is less than five years, a lump sum payment must be chosen.

(f) Termination Benefits

Members who terminate with fewer than five years of service receive a refund of their own contributions plus interest.

Members who terminate with more than five years of service and are not immediately entitled to a pension may apply for a deferred pension.

(g) Province's Liability for Benefits

The Province of Alberta is liable to pay all benefits not paid by the plan.

(h) Prior Service and Transfers

All prior service purchases are to be cost-neutral to the plan.

All existing reciprocal agreements were terminated in 1994. New reciprocal agreements were or are being renegotiated to provide that transferred-in service be on an actuarial reserve basis and transfers out receive the greater of the termination benefits or commuted value for all service.

(i) Cost-of-Living Adjustments

Pensions payable are increased each year by an amount equal to at least 60% of the increase in the Alberta Consumer Price Index.

(j) Income Taxes

The plan is a registered pension plan as defined in the *Income Tax Act* and is not subject to income taxes. The plan's registration number is 0927764.

Note 2 Summary of Significant Accounting Policies and Reporting Practices

(a) Basis of Presentation

These financial statements are prepared on the going concern basis in accordance with generally accepted accounting principles. The statements provide information about the net assets available in the plan to meet future benefit payments and are prepared to assist plan members and others in reviewing the activities of the plan for the year. They do not reflect the funding requirements of the plan or the benefit security of individual members.

The majority of plan investments are held in pooled investment funds administered by Alberta Treasury. Pooled investment funds have a market-based unit value that is used to allocate income to members and to value purchases and sales of pool units.

The plan's respective percentage ownership in pooled investment funds at March 31 was as follows:

| | % Ownership | |
|---|---|---|
| | 1999 | 1998 |
| Canadian Dollar Public Bond Pool | 0.4 | 0.4 |
| Canadian Pooled Equities Fund | 0.5 | 0.5 |
| Domestic Passive Equity Pooled Fund | 0.5 | |
| External Managers Fund | 0.3 | 0.4 |
| Global Structured Equity Pooled Fund | 0.2 | 0.4 |
| Private Bond Pool | - | 0.4 |
| Private Equity Pool | 0.6 | 0.6 |
| Private Mortgage Pool | 0.3 | 0.4 |
| Private Real Estate Pool | 0.4 | 0.1 |
| Transition Account | - | 0.6 |
| United States Pooled Equities Fund | 0.4 | 0.4 |
| US Passive Equity Pooled Fund | 0.4 | 0.4 |

(b) Valuation of Assets and Liabilities

Investments are stated at fair value. The methods used to determine the fair value of investments held either by the plan or by pooled investment funds are explained in the following paragraphs.

Short-term securities, public fixed income securities and equities are valued at the year-end closing sale price or the average of the latest bid and ask prices quoted by an independent securities valuation company.

Private fixed income securities and mortgages are valued based on the net present value of future cash flows. These cash flows are discounted using Government of Canada bond rates adjusted for a risk premium estimated by management.

The fair value of private equities is estimated by management.

Real estate investments are reported at their most recent appraised value, net of any liabilities against the real property. Real estate properties are appraised annually by qualified external real estate appraisers.

The fair values of deposits, receivables, accrued investment income and payables are estimated to approximate their book values.

(c) Income Recognition

Dividends are accrued on the ex-dividend date. Income from other investments is accrued as earned. Gains or losses on investments are recognized concurrently with changes in fair value.

(d) Foreign Exchange

Foreign currency transactions are translated into Canadian dollars using average rates of exchange, except for hedged foreign currency transactions which are translated at rates of exchange established by the terms of the forward exchange contracts. At the year-end, the fair value of investments and any other assets and liabilities denominated in a foreign currency are translated at the year-end exchange rate. Exchange differences are included in the determination of investment income.

(e) Derivative Financial Instruments

Income and expense on index swaps and interest rate swaps are accrued as earned and included in investment income. Gains and losses on forward foreign exchange contracts are recognized concurrently with changes in fair value.

Note 3 Investments (Schedules A to D)

Investments are summarized as follows:

| | 1999 | | 1998 | |
|---|---|---|---|---|
| | ($ thousands) | % | ($ thousands) | % |
| Deposit in the Consolidated Cash Investment Trust Fund (a) | $ 4,032 | 5.0 | $ 1,788 | 2.3 |
| Fixed Income Securities | | | | |
| Canadian Dollar Public Bond Pool (Schedule A) | 30,538 | 37.7 | 28,772 | 36.8 |
| Private Mortgage Pool (b) | 2,816 | 3.5 | 2,910 | 3.7 |
| Private Bond Pool | - | - | 3,309 | 4.2 |
| Total deposits and fixed income securities | 37,386 | 46.2 | 36,779 | 47.0 |
| Canadian Equities | | | | |
| Canadian Pooled Equities Fund (Schedule B) | 10,981 | 13.6 | 11,774 | 15.0 |
| Transition Account | - | - | 10,732 | 13.7 |
| Domestic Passive Equity Pooled Fund (Schedule C) | 9,578 | 11.8 | - | - |
| External Managers Fund (Canadian) (Schedule D) | 2,769 | 3.4 | 1,256 | 1.6 |
| Private Equity Pool (c) | 462 | 0.6 | 763 | 1.0 |
| | 23,790 | 29.4 | 24,525 | 31.3 |
| Foreign Equities | | | | |
| External Managers Fund (Global) (Schedule D) | 9,407 | 11.6 | 8,617 | 11.0 |
| Global Structured Equity Pooled Fund (d) | 3,054 | 3.8 | 3,813 | 4.9 |
| US Passive Equity Pooled Fund (e) | 2,335 | 2.9 | 1,994 | 2.5 |
| External Managers Fund (United States) (Schedule D) | 2,359 | 2.9 | 1,891 | 2.4 |
| United States Pooled Equities Fund | 37 | - | 161 | 0.2 |
| | 17,192 | 21.2 | 16,476 | 21.0 |
| Equities in Real Estate | | | | |
| Private Real Estate Pool (f) | 2,572 | 3.2 | 553 | 0.7 |
| Total equities | 43,554 | 53.8 | 41,554 | 53.0 |
| Total investments | $ 80,940 | 100.0 | $ 78,333 | 100.0 |

(a) The Consolidated Cash Investment Trust Fund is managed with the objective of providing competitive interest income to depositors while maintaining maximum security and liquidity of depositors' capital. The portfolio is comprised of high quality short-term and mid-term fixed income securities with a maximum term to maturity of five years.

(b) The Private Mortgage Pool is managed with the objective of providing investment returns higher than attainable from the publicly traded bond market over the long term. The portfolio is comprised primarily of high quality commercial mortgage loans. In order to reduce risk, the pool only invests in loans insured by a federal agency and first-mortgage loans that provide diversification by property usage. The pool does not invest in mortgages on single family houses, hotels, motels, trailer parks or recreational properties. As at March 31, 1999, mortgages held by the pool have an average effective yield of 7.08% per annum based on market (1998: 7.37%). Approximately 84% of the mortgages held will mature within ten years (1998: 90%).

(c) The Private Equity Pool is managed with the objective of providing investment returns higher than attainable from publicly traded equity indices such as the Toronto Stock Exchange 300 Index over the long term. The portfolio is comprised of equity investments in companies that show higher than average growth potential. Risk is reduced by avoiding direct investments in start-up and venture capital situations and by limiting holdings in any single company.

(d) The Global Structured Equity Pooled Fund is managed with the objective of providing investment returns comparable to the total return of the Morgan Stanley Capital International World Index. The pooled fund provides exposure to global markets through the use of structured investments such as foreign equity index swaps and interest rate swaps.

(e) The US Passive Equity Pooled Fund is managed with the objective of attaining investment returns comparable to Standard & Poor's (S & P) 500 Index. The portfolio is comprised of publicly traded equities in the United States similar in weights to the S & P 500 Index. To enhance investment returns with no substantial increase in risks, the pooled fund also invests in futures, swaps and other structured investments.

(f) The Private Real Estate Pool is managed with the objective of providing investment returns comparable to the Russell Canadian Property Index over the long term. Real estate is held through intermediate companies, which have issued to the pool common shares and participating debentures secured by a charge on real estate. Risk is reduced by investing in properties that provide diversification by geographic location, by property type and by tenancy. As real estate returns are positively correlated to inflation and negatively correlated to returns from fixed income securities and equities, the pool provides diversification from the securities market with opportunities for high returns.

Note 4 Investment Risk Management

Fair values of investments are exposed to credit risk and price risk. Credit risk relates to the possibility that a loss may occur from the failure of another party to perform according to the terms of a contract. Price risk is comprised of currency risk, interest rate risk and market risk. Currency risk relates to the possibility that the investments will change in value due to future fluctuations in foreign exchange rates. Interest rate risk relates to the possibility that the investments will change in value due to future fluctuations in market interest rates. Market risk relates to the possibility that the investments will change in value due to future fluctuations in market prices.

Actuarial liabilities of the plan are primarily affected by the long-term real rate of return on investments. In order to earn the best possible return at an acceptable level of risk, management has established a policy asset mix benchmark of 50% fixed income instruments and 50% equities. Risk is reduced through asset class diversification, diversification within each asset class, quality constraints on fixed income instruments and restrictions on amounts exposed to countries designated as emerging markets. Borrowing or leveraging is not allowed with the exception of pre-existing mortgages on real estate properties. Controls are in place respecting the use of derivatives (see Note 5). Forward foreign exchange contracts are used to manage currency exposure in connection with securities purchased in foreign currency.

Note 5 Derivatives: Index Swaps, Interest Rate Swaps, Foreign Exchange Contracts and Stock Index Futures Contracts

Pooled funds use index and interest rate swaps to enhance return. A swap is a contractual agreement between two parties to exchange a series of cash flows based on a notional amount and does not involve the exchange of the underlying principal.

An index swap involves the exchange of a floating interest rate cash flow for one based on the performance of a market index. For interest rate swaps, parties generally exchange fixed and floating rate interest cash flows based on a notional value. There are underlying securities supporting all swaps. Leveraging is not allowed.

The following is a summary of the plan's proportionate share of the notional value of index and interest rate swaps held or issued by pooled funds at March 31, 1999.

| | 1999 | 1998 |
|---|---|---|
| | ($ thousands) | |
| Index swaps | | |
| Bonds - Canadian Dollar Public Bond Pool | $ 5,730 | $ 5,232 |
| Canadian equities | | |
| Domestic Passive Equity Pooled Fund | 3,662 | - |
| Transition Account | - | 1,366 |
| Foreign equities | | |
| Global Structured Equity Pooled Fund | 3,002 | 3,743 |
| US Passive Equity Pooled Fund | 2,305 | 1,883 |
| Interest Rate Swaps | | |
| Fixed to floating | | |
| Canadian Dollar Public Bond Pool | 4,118 | 2,619 |
| Domestic Passive Equity Pooled Fund | 2,782 | - |
| Global Structured Equity Pooled Fund | 2,138 | 2,147 |
| US Passive Equity Pooled Fund | 209 | - |
| Transition Account | - | 450 |
| | $ 23,946 | $ 17,440 |

Fair values of swaps have been included in the determination of the fair values of the respective pooled investment funds. Credit exposure relating to swaps is minimal as management deals only with counterparties rated not less than AA.

Foreign exchange contracts are contractual agreements to exchange specified currencies at an agreed upon exchange rate and on an agreed settlement date in the future. As at March 31, 1999, the plan's proportionate share of outstanding forward foreign exchange contracts issued by the External Managers Fund amounted to $2,314,000 (1998: $1,575,000).

Stock index futures contracts are contractual agreements to pay or receive specified currencies based on the variances of a specified stock index between an agreed level and the actual level on an agreed date in the future. As at March 31, 1999, the plan's proportionate share of outstanding stock index futures contracts issued by the External Managers Fund amounted to $100,000 (1998: $Nil).

Note 6 Accrued Benefits

(a) Actuarial Valuation

An actuarial valuation of the plan was carried out as at March 31, 1999 by Crouse Dorgan Consultants Inc. The March 31, 1999 valuation resulted in an actuarial surplus of $18.9 million as disclosed in the Statement of Net Assets Available for Benefits and Accrued Benefits.

The valuation as at March 31, 1999 was determined using the projected benefit method, based on service. The assumptions used in the valuation were developed as the best estimate of expected short-term and long-term market conditions and other future events. This estimate was, after consultation with the plan's actuary, adopted by management.

The major assumptions used were:

| | December 31 | |
|---|---|---|
| | 1999 Valuation | 1998 Valuation |
| | % | % |
| Asset real rate of return | 3.5 | 3.5 |
| Inflation rate | 3.5 | 3.5 |
| Investment return | 7.0 | 7.0 |
| Salary escalation rate (after phasing-in) | 4.0 | 4.0 |
| Pension cost of living increase as a percentage of Alberta Consumer Price Index | 60 | 60 |

The following statement shows the principal components of the change in the value of accrued pension benefits. The periods presented coincide with the performance of the actuarial valuations carried out at March 31, 1995, 1998 and 1999.

| | Year Ended March 31, 1999 | Three Years Ended March 31, 1998 |
|---|---|---|
| | ($ thousands) | |
| Accrued pension benefits, beginning of period | $ 53,717 | $ 44,495 |
| Interest accrued on benefits | 3,869 | 10,013 |
| Net experience losses (gains) | 5,651 | (2,590) |
| Changes in actuarial assumptions | - | 3,659 |
| Benefits earned | 1,553 | 3,986 |
| Benefits paid | (2,528) | (5,846) |
| Accrued pension benefits, end of period | $ 62,262 | $ 53,717 |

(b) Sensitivity of Changes in Major Assumptions

The plan's future experience will inevitably differ, perhaps significantly, from these assumptions. Any differences between the actuarial assumptions and future experience will emerge as gains or losses in future valuations and will affect the financial position of the plan.

As at March 31, 1999, holding the nominal investment return and salary escalation assumptions constant, a 1% increase in the assumed long-term inflation rate would result in an increase in the value of accrued benefits by approximately $3.4 million.

As at March 31, 1999, holding the long-term inflation rate and nominal investment return assumptions constant, a 1% increase in the assumed salary escalation rate would result in an increase in the value of accrued benefits by approximately $0.5 million.

As at March 31, 1999, holding the long-term inflation rate and salary escalation assumptions constant, a 1% increase in the assumed real long-term investment return would result in a decrease in the value of accrued benefits by approximately $6.1 million.

Note 7 Actuarial Surplus

The plan surplus may be used to reduce contributions required under the plan, or it may be returned to the Province by an order of the Lieutenant Governor in Council.

Note 8 Investment Income

| | 1999 | | | 1998 |
|---|---|---|---|---|
| | Income (a) | Change in Fair Value | Total | Total |
| | ($ thousands) | | | |
| Deposits and Fixed Income Securities: | | | | |
| Deposit in the Consolidated Cash Investment Trust Fund | $ 61 | $ - | $ 61 | $ 72 |
| Canadian Dollar Public Bond Pool | 1,907 | 117 | 2,024 | 3,632 |
| Private Debt Pool | 140 | (43) | 97 | 177 |
| Private Mortgage Pool | 199 | (23) | 176 | 299 |
| | 2,307 | 51 | 2,358 | 4,180 |
| Equities: | | | | |
| Canadian Pooled Equities Fund | 221 | (1,134) | (913) | 3,593 |
| Transition Account | 38 | (22) | 16 | 1,139 |
| Domestic Passive Equity Pooled Fund | (230) | (1,006) | (1,236) | - |
| External Managers Fund (Canadian) | 23 | (1,462) | (1,439) | 299 |
| Private Equity Pool | 4 | (79) | (75) | 82 |
| External Managers Fund (Global) | 144 | 2,454 | 2,598 | 1,405 |
| Global Structured Equity Pooled Fund | 430 | 59 | 489 | 740 |
| US Passive Equity Pooled Fund | 446 | 67 | 513 | 93 |
| External Managers Fund (United States) | 13 | 594 | 607 | 687 |
| United States Pooled Equities Fund | - | (51) | (51) | 743 |
| Private Real Estate Pool | 104 | 95 | 199 | 95 |
| | 1,193 | (485) | 708 | 8,876 |
| | $ 3,500 | $ (434) | $ 3,066 | $ 13,056 |

(a) Income is comprised of dividends, interest and rental income less custodial and pooled fund management fees, which have been deducted in arriving at income.

Note 9 Administration Expenses

Accommodation and certain administration costs, including salaries, benefits and telecommunication services incurred on behalf of the plan by the Government of Alberta have not been included in the plan's expenses. These costs, which are not considered material to the plan, are recorded by the Government of Alberta and are not recovered from the plan.

Note 10 Budget Information

The accrued benefits are based on management's best estimates of future events after consultation with the plan's actuary. Differences between actual results and management's expectations are disclosed as experience gains or losses in Note 6. Accordingly, a budget is not included in these financial statements.

Note 11 Uncertainty Due to the Year 2000

The year 2000 issue is the result of some computer systems using two digits rather than four to define the applicable year. Computer systems that have date sensitive software may recognize a date using "00" as the year 1900 rather than the year 2000, which could result in miscalculations or system failures. In addition, similar problems may arise in some systems if certain dates in 1999 are not recognized as a valid date or are recognized to represent something other than a date. The effects of the year 2000 issue may be experienced before, on, or after January 1, 2000. If not addressed, the effect on operations and financial reporting may range from minor errors to significant systems failure that could affect the ability to conduct some operations. Despite efforts to address this issue, it is not possible to be certain that all aspects of the year 2000 issue affecting the plan, including those related to the efforts of suppliers and other third parties, will be fully resolved.

Note 12 Responsibility for Financial Statements

These financial statements were approved by management.

# PROVINCIAL JUDGES AND MASTERS IN CHAMBERS PENSION PLAN
## SCHEDULE OF INVESTMENTS IN CANADIAN DOLLAR PUBLIC BOND POOL (a) (b)
## MARCH 31, 1999

($ thousands)

| | 1999 | | 1998 | |
|---|---|---|---|---|
| | Plan's Share | Total Pool | Plan's Share | Total Pool |
| Deposit in the Consolidated Cash Investment Trust Fund | $ 430 | $ 114,298 | $ 367 | $ 89,415 |
| Public Fixed Income Securities | | | | |
| Government of Canada, direct and guaranteed | 8,396 | 2,230,533 | 9,913 | 2,412,052 |
| Provincial: | | | | |
| Alberta, direct and guaranteed | 727 | 193,244 | 823 | 200,176 |
| Other, direct and guaranteed | 3,983 | 1,058,095 | 4,782 | 1,163,671 |
| Municipal | 312 | 82,892 | 246 | 59,864 |
| Corporate | 12,086 | 3,210,563 | 12,373 | 3,010,460 |
| Private Fixed Income Securities | | | | |
| Corporate | 4,236 | 1,125,242 | - | - |
| Total deposit and fixed income securities | 30,170 | 8,014,867 | 28,504 | 6,935,638 |
| Receivable from sale of investments and accrued investment income | 744 | 197,596 | 492 | 119,799 |
| Liabilities for investment purchases | (376) | (99,845) | (224) | (54,526) |
| | 368 | 97,751 | 268 | 65,273 |
| | $ 30,538 | $ 8,112,618 | $ 28,772 | $ 7,000,911 |

(a) The Canadian Dollar Public Bond Pool is managed with the objective of providing competitive returns comparable to the total return of the Scotia Capital Markets Bond Universe Index over a four-year period while maintaining adequate security and liquidity of members' capital. The portfolio is comprised of high quality Canadian fixed income instruments and debt related derivatives. Competitive returns are achieved through management of the portfolio duration and sector rotation.

(b) Fixed income securities had an average effective current yield of 5.51% per annum based on market value (1998: 5.41% per annum). The following term structure of these securities as at March 31, 1999 is based on par value.

| | 1999 | 1998 |
|---|---|---|
| | % | |
| under 1 year | 10 | 13 |
| 1 to 5 years | 37 | 40 |
| 5 to 10 years | 24 | 19 |
| 10 to 20 years | 21 | 12 |
| over 20 years | 8 | 16 |
| | 100 | 100 |

Schedule B

# PROVINCIAL JUDGES AND MASTERS IN CHAMBERS PENSION PLAN
## SCHEDULE OF INVESTMENTS IN CANADIAN POOLED EQUITIES FUND (a)
### MARCH 31, 1999
($ thousands)

| | 1999 | | 1998 | |
|---|---|---|---|---|
| | Plan's Share | Total Pool | Plan's Share | Total Pool |
| Deposit in the Consolidated Cash Investment Trust Fund | $ 65 | $ 12,121 | $ 393 | $ 77,699 |
| Canadian Public Equities (b): | | | | |
| Common shares and rights: | | | | |
| Communications and media | 748 | 139,379 | 288 | 56,949 |
| Conglomerates | 615 | 114,522 | 710 | 140,403 |
| Consumer products | 529 | 98,452 | 387 | 76,582 |
| Financial services | 2,340 | 435,832 | 2,409 | 476,155 |
| Gold and precious minerals | 480 | 89,329 | 517 | 102,216 |
| Industrial products | 2,253 | 419,610 | 1,748 | 345,581 |
| Merchandising | 271 | 50,417 | 324 | 63,964 |
| Metals and minerals | 358 | 66,756 | 563 | 111,375 |
| Oil and gas | 824 | 153,484 | 1,745 | 344,978 |
| Paper and forest products | 220 | 40,913 | 328 | 64,847 |
| Pipelines | 287 | 53,368 | 294 | 58,225 |
| Real estate and construction | 264 | 49,262 | 209 | 41,374 |
| Transportation and environmental services | 276 | 51,555 | 536 | 105,919 |
| Utilities | 1,330 | 247,889 | 1,190 | 235,287 |
| Passive index | 144 | 26,883 | 104 | 20,525 |
| | 10,939 | 2,037,651 | 11,352 | 2,244,380 |
| Receivable from sale of investments and accrued investment income | 68 | 12,722 | 29 | 5,649 |
| Liabilities for investment purchases | (91) | (17,086) | - | - |
| | (23) | (4,364) | 29 | 5,649 |
| | $ 10,981 | $ 2,045,408 | $ 11,774 | $ 2,327,728 |

(a) The Canadian Pooled Equities Fund (CPE) is managed with the objective of providing returns higher than the total return of the Toronto Stock Exchange 300 index over a four-year period while maintaining preservation of members' capital. The portfolio is comprised of publicly traded equities in Canadian corporations. Risk is reduced by prudent security selection and sector rotation. During the last two years, a portion of the plan's investments held by the CPE was transferred to the Domestic Passive Equity Pooled Fund through the Transition Account.

(b) The industrial classifications are those used by the Toronto Stock Exchange.

Schedule C

# PROVINCIAL JUDGES AND MASTERS IN CHAMBERS PENSION PLAN
# SCHEDULE OF INVESTMENTS IN DOMESTIC PASSIVE EQUITY POOLED FUND (a)
# MARCH 31, 1999

($ thousands)

| | 1999 | |
|---|---|---|
| | Plan's Share | Total Pool |
| Deposit in the Consolidated Cash Investment Trust Fund | $ 32 | $ 6,772 |
| Short Term Securities | 61 | 12,790 |
| Floating Rate Note Pool | 3,108 | 650,930 |
| | 3,201 | 670,492 |
| Canadian Public Equities (b): | | |
| Common shares and rights: | | |
| Communications and media | 488 | 102,204 |
| Conglomerates | 181 | 37,986 |
| Consumer products | 263 | 55,059 |
| Financial services | 1,113 | 232,892 |
| Gold and precious minerals | 256 | 53,591 |
| Industrial products | 1,139 | 238,625 |
| Merchandising | 230 | 48,171 |
| Metals and minerals | 189 | 39,670 |
| Oil and gas | 542 | 113,447 |
| Paper and forest products | 170 | 35,617 |
| Pipelines | 149 | 31,167 |
| Real estate and construction | 127 | 26,571 |
| Transportation and environmental services | 120 | 25,232 |
| Utilities | 698 | 146,243 |
| Passive index | 97 | 20,212 |
| | 5,762 | 1,206,687 |
| Domestic Structured Equity Pooled Fund | 588 | 123,191 |
| United States Public Equities | 11 | 2,245 |
| Receivable from sale of investments and accrued investment income | 31 | 6,518 |
| Liabilities for investment purchases | (15) | (3,271) |
| | 16 | 3,247 |
| | $ 9,578 | $ 2,005,862 |

(a) The Domestic Passive Equity Pooled Fund is managed on a passive approach with the objective of providing investment returns comparable to the Toronto Stock Exchange (TSE) 300 Index. The portfolio is comprised of publicly traded Canadian equities and structured investments replicating the TSE 100 Index and the TSE 35 Index. A portion of the portfolio fully replicates the TSE 300. The other portion provides investment returns which are comparable to the TSE 100 Index and the TSE 35 Index through directly held swaps or investments in the Domestic Structured Equity Pooled Fund (DSEP). DSEP replicates the TSE 100 Index with index-based securities and structured investments such as index swaps and interest rate swaps. It provides returns comparable to the TSE 100 index. The Floating Rate Note Pool (FRNP) is managed with the objective of generating floating rate income needed for the swap obligations of the participants with structured investments in equities and bonds. Through the use of structured investments such as interest rate swaps, FRNP provides investment opportunities in high quality floating rate instruments with remaining term-to-maturity of ten years or less.

(b) The industrial classifications are those used by the Toronto Stock Exchange.

# PROVINCIAL JUDGES AND MASTERS IN CHAMBERS PENSION PLAN
# SCHEDULE OF INVESTMENTS IN EXTERNAL MANAGERS FUND (a) (b)
# MARCH 31, 1999

($ thousands)

| | 1999 | | 1998 | |
|---|---|---|---|---|
| | Plan's Share | Total Pool | Plan's Share | Total Pool |
| Foreign Public Equity Pools | | | | |
| Multi Region | $ 4,309 | $ 1,086,288 | $ 3,956 | $ 966,692 |
| Europe | 2,986 | 801,758 | 3,032 | 744,800 |
| Pacific Basin | 1,951 | 522,234 | 1,629 | 403,452 |
| Emerging Markets | 161 | 51,304 | - | - |
| | 9,407 | 2,461,584 | 8,617 | 2,114,944 |
| United States | 2,359 | 639,590 | 1,891 | 473,221 |
| Canadian Public Equity Pools | | | | |
| Large Cap | 1,752 | 800,564 | - | - |
| Small Cap | 1,017 | 437,043 | 1,256 | 455,795 |
| | 2,769 | 1,237,607 | 1,256 | 455,795 |
| | $ 14,535 | $ 4,338,781 | $ 11,764 | $ 3,043,960 |

(a) The External Managers Fund is managed by external managers with expertise in global and Canadian equity markets. The objective of the fund is to provide investment returns higher than the total return of the applicable Morgan Stanley Capital International, Standard & Poor and Toronto Stock Exchange indices over a four-year period. The portfolio is comprised of publicly traded equity securities on Canadian and approved foreign markets. Risk is reduced through manager, style and market diversification.

(b) The following is a summary of assets and liabilities of the External Managers Fund as at March 31, 1999:

| | 1999 | 1998 |
|---|---|---|
| | ($ thousands) | |
| Cash and short-term securities | $ 109,079 | $ 130,426 |
| Receivables from sale of investments and accrued investment income | 27,890 | 27,357 |
| Investments | | |
| Public equities | 4,239,151 | 2,915,747 |
| Convertible bonds | 1,302 | 3,408 |
| Liability for investment purchases | (38,641) | (32,978) |
| | $ 4,338,781 | $ 3,043,960 |

# PUBLIC SERVICE MANAGEMENT (CLOSED MEMBERSHIP) PENSION PLAN FINANCIAL STATEMENTS DECEMBER 31, 1998



## AUDITOR'S REPORT

To the Provincial Treasurer

I have audited the statement of accrued pension benefits and net assets available for benefits of the Public Service Management (Closed Membership) Pension Plan as at December 31, 1998 and the statement of changes in net assets available for benefits for the year then ended. These financial statements are the responsibility of the Plan's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In my opinion, these financial statements present fairly, in all material respects, the financial position of the Plan as at December 31, 1998 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles.

Peter Valentine, FCA
Auditor General

Edmonton, Alberta
April 19, 1999

## PUBLIC SERVICE MANAGEMENT (CLOSED MEMBERSHIP) PENSION PLAN
## STATEMENT OF ACCRUED BENEFITS AND
## NET ASSETS AVAILABLE FOR BENEFITS
## AS AT DECEMBER 31, 1998

($ thousands)

| | 1998 | 1997 |
|---|---|---|
| **Accrued Benefits** | | |
| Actuarial value of accrued pension benefits (Note 6) | $ 657,524 | $ 666,324 |
| **Net Assets Available for Benefits** | | |
| Assets | | |
| Cash and short-term securities (Note 3) | 5,154 | 21,523 |
| Accounts receivable | - | 6 |
| | 5,154 | 21,529 |
| Liabilities | | |
| Accounts payable (Note 4) | 58 | - |
| Net assets available for benefits | 5,096 | 21,529 |
| Excess of actuarial value of accrued pension benefits over net assets | $ 652,428 | $ 644,795 |

*See accompanying notes.*

## PUBLIC SERVICE MANAGEMENT (CLOSED MEMBERSHIP) PENSION PLAN
## STATEMENT OF CHANGES IN NET ASSETS AVAILABLE FOR BENEFITS
## FOR THE YEAR ENDED DECEMBER 31, 1998

($ thousands)

| | 1998 | 1997 |
|---|---|---|
| Increase in assets | | |
| Investment income | $ 381 | $ 1,152 |
| Contributions from the Province of Alberta (Note 1(b)) | 40,000 | 60,000 |
| Transfers from other plans and past service contributions | 1 | (3) |
| Total increase in assets | 40,382 | 61,149 |
| Decrease in assets | | |
| Pension benefits | 56,557 | 56,233 |
| Refunds to members | 53 | 124 |
| Transfers to other plans | 50 | - |
| Administration expenses (Note 5) | 155 | 106 |
| Total decrease in assets | 56,815 | 56,463 |
| Increase (Decrease) in net assets for the year | (16,433) | 4,686 |
| Net assets available for benefits at beginning of year | 21,529 | 16,843 |
| Net assets available for benefits at end of year | $ 5,096 | $ 21,529 |

*See accompanying notes.*

# PUBLIC SERVICE MANAGEMENT (CLOSED MEMBERSHIP) PENSION PLAN
## NOTES TO THE FINANCIAL STATEMENTS
## DECEMBER 31, 1998

Note 1 Summary Description of the Plan

The following description of the Public Service Management (Closed Membership) Pension Plan is a summary only. For a complete description of the plan, reference should be made to the *Public Sector Pension Plans Act*, Chapter P-30.7, Statutes of Alberta 1993.

(a) General

The Public Service Management (Closed Membership) Pension Plan is a defined benefit pension plan for eligible retired management employees of the Province of Alberta and certain provincial agencies and public bodies. Members of the former Public Service Management Pension Plan who were retired, were entitled to receive deferred pensions or had attained 35 years of service before August 1, 1992, continue as members of this plan.

(b) Funding

The plan is funded by investment income and money appropriated to the plan, if any, by the Province of Alberta Legislature.

The plan's actuary performs an actuarial valuation of the plan at least once every three years.

(c) Retirement Benefits

The plan provides for a pension of 2.0% for each year of pensionable service based on the average salary of the highest five consecutive years. The maximum service allowable under the plan is 35 years.

Members are entitled to receive a pension if they terminated before August 1, 1992 and attained age 55 with at least five years of service. In addition, those members who had achieved 35 years of service at August 1, 1992 and subsequently terminated are also entitled to a pension.

(d) Guarantee

The Province of Alberta guarantees payment of all benefits arising under the plan. After all assets in the plan are exhausted, the Province of Alberta pays all benefits under the plan and the plan costs.

(e) Cost-of-Living Adjustments

Pensions payable by the plan are increased each year by an amount equal to at least 60 percent of the increase in the Alberta Consumer Price Index.

(f) Income Taxes

The plan is a registered pension plan as defined in the *Income Tax Act*, and is not subject to income taxes. The plan's registration number is 0570887.

Note 2 Summary of Significant Accounting Policies and Reporting Practices

(a) Basis of Presentation

These financial statements are prepared on the going concern basis in accordance with generally accepted accounting principles. The statements provide information about the net assets available in the plan to meet future benefit payments, and are prepared to assist plan members and others in reviewing the activities of the plan for the year. They do not reflect the funding requirements of the plan or the benefit security of individual participants.

(b) Valuation of Assets and Liabilities

Investments are stated at fair value. Short-term securities are valued at the year-end closing sale price or the average of the latest bid and ask prices quoted by an independent securities valuation company.

The fair values of deposits, receivables, accrued investment income and payables are estimated to approximate their book values.

(c) Income Recognition

Investment income is accrued as earned. Gains or losses on investments are recognized concurrently with changes in fair value.

Note 3 Cash and Short-term Securities

Cash and short-term securities consist primarily of deposits in the Consolidated Cash Investment Trust Fund. The fund is managed with the objectives of providing competitive interest income to depositors while maintaining maximum security and liquidity of depositors' capital. The portfolio is comprised of high-quality short-term and mid-term fixed income securities with a maximum term to maturity of five years.

Note 4 Accounts Payable

| | 1998 | 1997 |
|---|---|---|
| | ($ thousands) | |
| Benefits | $ 1 | $ - |
| Administration expenses | 57 | - |
| | $ 58 | $ - |

Note 5 Administration Expenses

| | 1998 | 1997 |
|---|---|---|
| | ($ thousands) | |
| General administration costs | $ 147 | $ 101 |
| Actuarial fees | - | 4 |
| Investment management costs | 8 | 1 |
| | $ 155 | $ 106 |

General administration costs, including the board costs, were paid to Alberta Pensions Administration Corporation on a cost-recovery basis.

Investment management costs were paid to Alberta Treasury, and do not include custodial fees, which have been deducted in arriving at investment income.

Total administration expenses amounted to $56 per member (1997: $37 per member). The $19 per member cost increase in 1998 is attributed to the following factors: changes in the accounting treatment of business process reengineering cost $7, increase in general operations cost $10, increase in investment management cost $3, and decrease in plan specific cost ($1).

Note 6 Actuarial Value of Accrued Benefits

(a) Actuarial Valuation

An actuarial valuation of the plan was carried out as at December 31, 1996 by William M. Mercer Limited and was then extrapolated to December 31, 1998. The December 31, 1996 valuation resulted in an actuarial deficiency of $657 million.

The valuation as at December 31, 1996 was determined using the projected benefit method prorated on service. The assumptions used in the valuation were developed by reference to the Management Employees Pension Board's best estimate of expected short-term and long-term market conditions and other future events. The major assumptions used were:

| | December 31, | |
|---|---|---|
| | 1998 Extrapolation | 1996 Valuation |
| | % | % |
| Asset real rate of return | 4.0 | 4.0 |
| Inflation rate (after phasing-in) | 3.5 | 3.5 |
| Investment rate of return | 7.5 | 7.5 |
| Pension cost-of-living increase as a percentage of Alberta Consumer Price Index | 60.0 | 60.0 |

The following statement shows the principal components of the change in the value of accrued benefits. The periods presented coincide with the performance of the actuarial valuations carried out at December 31, 1994 and 1996 and extrapolation made at December 31, 1998.

| | Two Years Ended December 31, 1998 | Two Years Ended December 31, 1996 |
|---|---|---|
| | ($ thousands) | |
| Actuarial value of accrued benefits at beginning of period | $ 673,724 | $ 671,424 |
| Net experience losses | - | 7,900 |
| Interest accrued on benefits | 101,000 | 113,100 |
| Changes in actuarial assumptions | - | 2,400 |
| Net benefits paid, including interest | (117,200) | (121,100) |
| Actuarial value of accrued benefits at end of period | $ 657,524 | $ 673,724 |

(b) Sensitivity of Changes in Major Assumptions

The plan's future experience will inevitably differ, perhaps significantly, from these assumptions. Any differences between the actuarial assumptions and future experience will emerge as gains and losses in future valuations and will affect the financial position of the plan.

As at December 31, 1998, holding the nominal investment return assumption constant, a 1% increase in the assumed long-term inflation rate would result in an increase in the deficiency of the plan from $652 million to $698 million.

As at December 31, 1998, holding the inflation rate assumption constant, a 1% increase in the assumed long-term investment return would result in a decrease in the deficiency of the plan from $652 million to $601 million.

Note 7 Budget Information

The accrued benefits are based on the Management Employees Pension Board's best estimate of future events. Differences between actual results and management's expectations are disclosed as net experience gains and losses in Note 6. Accordingly, a budget is not included in these financial statements.

Note 8 Uncertainty Due to the Year 2000

The year 2000 issue is the result of some computer programs being written using two digits rather than four to define the applicable year. Computer programs that have date sensitive software may recognize a date using "00" as the year 1900 rather than the year 2000, which could result in miscalculations or system failures. In addition, similar problems may arise in some systems if certain dates in 1999 are not recognized as a valid date or are recognized to represent something other than a date. The effects of the year 2000 issue may be experienced before, on, or after January 1, 2000. If not addressed, the effect on operations and financial reporting may range from minor errors to significant systems failure that could affect the ability to conduct some operations. Despite efforts to address this issue, it is not possible to be certain that all aspects of the year 2000 issue affecting the plan, including those related to the efforts of suppliers and other third parties, will be fully resolved.

Note 9 Responsibility for Financial Statements

These financial statements were prepared by management and approved by the Management Employees Pension Board.

PUBLIC SERVICE PENSION PLAN
FINANCIAL STATEMENTS
DECEMBER 31, 1998



## Auditor’s Report

To the Public Service Pension Board

I have audited the statement of net assets available for benefits and liability for accrued benefits of the Public Service Pension Plan as at December 31, 1998 and the statements of changes in net assets available for benefits, changes in liability for accrued benefits and changes in actuarial surplus for the year then ended. These financial statements are the responsibility of the Plan's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In my opinion, these financial statements present fairly, in all material respects, the financial position of the Plan as at December 31, 1998 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles.

Peter Valentine, FCA
Auditor General

Edmonton, Alberta
September 16, 1999

## PUBLIC SERVICE PENSION PLAN
## STATEMENT OF NET ASSETS AVAILABLE FOR BENEFITS AND LIABILITY FOR ACCRUED BENEFITS AS AT DECEMBER 31, 1998

($ thousands)

| | 1998 | 1997 |
|---|---|---|
| **Net Assets Available for Benefits** | | |
| Assets | | |
| Investments (Note 3) | $ 3,603,705 | $ 3,331,693 |
| Accounts receivable (Note 6) | 12,382 | 10,244 |
| | 3,616,087 | 3,341,937 |
| Liabilities | | |
| Accounts payable | 1,642 | 1,128 |
| Net assets available for benefits | 3,614,445 | 3,340,809 |
| Actuarial asset fluctuation reserve [Note 2 (c )] | (87,000) | (191,000) |
| Actuarial value of net assets available for benefits | 3,527,445 | 3,149,809 |
| **Liability for Accrued Benefits** | | |
| Liability for accrued benefits (Note 7) | 3,121,000 | 2,979,000 |
| Actuarial surplus (Note 7) | $ 406,445 | $ 170,809 |

*See accompanying notes and schedules.*

## PUBLIC SERVICE PENSION PLAN
## STATEMENT OF CHANGES IN NET ASSETS AVAILABLE FOR BENEFITS FOR THE YEAR ENDED DECEMBER 31, 1998

($ thousands)

| | 1998 | 1997 |
|---|---|---|
| Increase in assets | | |
| Investment income (Note 8) | $ 297,352 | $ 385,820 |
| Contributions | | |
| Current and past service | | |
| Employers | 60,886 | 56,491 |
| Employees | 62,323 | 58,042 |
| Pre-1992 unfunded liability | | |
| Employers | 3,645 | 3,461 |
| Employees | 3,645 | 3,461 |
| Province of Alberta | 12,150 | 11,538 |
| Transfers from other plans | 154 | 434 |
| | 142,803 | 133,427 |
| Total increase in assets | 440,155 | 519,247 |
| Decrease in assets | | |
| Pension benefits | 137,127 | 132,491 |
| Refunds to members | 24,795 | 27,111 |
| Transfers to other plans | 594 | 480 |
| Administration expenses (Note 9) | 4,003 | 2,905 |
| Total decrease in assets | 166,519 | 162,987 |
| Net increase in net assets for the year | 273,636 | 356,260 |
| Net assets available for benefits at beginning of year | 3,340,809 | 2,984,549 |
| Net assets available for benefits at end of year | $ 3,614,445 | $ 3,340,809 |

*See accompanying notes and schedules.*

## PUBLIC SERVICE PENSION PLAN
## STATEMENT OF LIABILITY FOR ACCRUED BENEFITS
## FOR PERIODS ENDED DECEMBER 31, 1998

($ thousands)

| | Year ended December 31, 1998 | | | Two years ended December 31, 1997 |
|---|---|---|---|---|
| | Pre-1992 | Post-1991 | Total | Total |
| Increase in liability for accrued benefits | | | | |
| Interest accrued on benefits | $ 163,000 | $ 62,000 | $ 225,000 | $ 437,000 |
| Benefits earned | - | 103,000 | 103,000 | 221,000 |
| Increase in liability for accrued benefits | 163,000 | 165,000 | 328,000 | 658,000 |
| Decrease in liability for accrued benefits | | | | |
| Benefits paid | 136,000 | 27,000 | 163,000 | 318,000 |
| Experience gains (losses) | - | (43,000) | (43,000) | 11,500 |
| Changes in actuarial assumptions | 41,000 | 25,000 | 66,000 | 81,000 |
| Decrease in liability for accrued benefits | 177,000 | 9,000 | 186,000 | 410,500 |
| Net increase (decrease) in liability for accrued benefits | (14,000) | 156,000 | 142,000 | 247,500 |
| Liability for accrued benefits at beginning of period | 2,242,600 | 736,400 | 2,979,000 | 2,731,500 |
| Liability for accrued benefits at end of period (Note 7) | $ 2,228,600 | $ 892,400 | $ 3,121,000 | $ 2,979,000 |

*See accompanying notes and schedules.*

## PUBLIC SERVICE PENSION PLAN
## STATEMENT OF CHANGES IN ACTUARIAL SURPLUS
## FOR PERIODS ENDED DECEMBER 31, 1998

($ thousands)

| | Year ended December 31, 1998 | | | Two years ended December 31, 1997 |
|---|---|---|---|---|
| | Pre-1992 | Post-1991 | Total | Total |
| Actuarial surplus (deficiency) at beginning of period | $ (95,600) | $ 266,409 | $ 170,809 | $ (231,121) |
| Net increase in net assets available for benefits | 81,445 | 192,191 | 273,636 | 761,430 |
| Net decrease (increase) in actuarial asset fluctuation reserve | 76,000 | 28,000 | 104,000 | (112,000) |
| Net decrease (increase) in liability for accrued benefits | 14,000 | (156,000) | (142,000) | (247,500) |
| Actuarial surplus at end of period | $ 75,845 | $ 330,600 | $ 406,445 | $ 170,809 |

*See accompanying notes and schedules*

# PUBLIC SERVICE PENSION PLAN
# NOTES TO THE FINANCIAL STATEMENTS
# DECEMBER 31, 1998

Note 1 Summary Description of the Plan

The following description of the Public Service Pension Plan is a summary only. For a complete description of the plan, reference should be made to the *Public Sector Pension Plans Act,* Chapter P-30.7, Statutes of Alberta 1993 and Alberta Regulation 368/93.

(a) General

The Public Service Pension Plan is a contributory defined benefit pension plan for eligible employees of the Province of Alberta, approved provincial agencies and public bodies, including universities and local boards of health units established under the *Public Health Act* and the Special Areas Board.

(b) Funding

Current service costs are funded equally by employers and employees at rates which are expected to provide for all benefits payable under the plan. The rates in effect are 4.675% of pensionable salary up to the Canada Pension Plan's Year's Maximum Pensionable Earnings (YMPE) and 6.55% for the excess. The rates are to be reviewed at least once every three years by the board based on recommendations of the plan's actuary.

The unfunded liability for service prior to January 1, 1992 was being financed by additional contributions in the ratio of 62.5% by the Province of Alberta and 18.75% each by employers and employees [see Note 7 (a)]. The rates were set on the basis that the additional contributions would eliminate the unfunded liability on or before December 31, 2036. The rates in effect, based on pensionable salary, were 1.0% for the Province of Alberta and 0.30% each for employers and employees.

(c) Retirement Benefits

The plan provides for a pension of 1.4% for each year of pensionable service based on average salary of the highest five consecutive years up to the YMPE and 2.0% on the excess. The maximum service allowable under the plan is 35 years. Pensions are payable to members who retire with at least five years of service and either have attained age 65 or have attained age 55 and the sum of their age and years of service equals 85. Reduced pensions are payable to members age 55 retiring early with a minimum of five years of service.

(d) Termination Benefits

Members who terminate with at least five years of service and are not immediately entitled to a pension may receive a refund of their contributions and interest on service prior to 1992 and commuted value for service after 1991, subject to lock-in provisions. Alternatively, they may elect to receive a deferred pension. Members who terminate with less than five years of service receive a refund of their contributions and interest.

(e) Disability Benefits

Unreduced pensions are payable to members who become totally disabled and have at least five years of service. Reduced pensions are payable to members who become partially disabled and have at least five years of service.

(f) Death Benefits

Death benefits are payable on the death of a member. If the member has at least five years of service, a surviving spouse may choose to receive a survivor pension. For a beneficiary other than a spouse or where service is less than five years, a lump sum payment must be chosen.

(g) Prior Service and Transfers

All prior service purchases are to be made on a basis that is cost-neutral to the plan.

All reciprocal agreements provide that transferred-in service be on an actuarial reserve basis and transfers-out receive the greater of the termination benefits or commuted value for all service.

(h) Cost-of-Living Adjustments

Pensions payable are increased each year by an amount equal to at least 60% of the increase in the Alberta Consumer Price Index.

(i) Income Taxes

The plan is a registered pension plan as defined in the *Income Tax Act* and the plan is not subject to income taxes. The plan's registration number is 0208769.

Note 2 Summary of Significant Accounting Policies and Reporting Practices

(a) Basis of Presentation

These financial statements are prepared on the going concern basis in accordance with generally accepted accounting principles. The statements provide information about the net assets available in the plan to meet future benefit payments and are prepared to assist plan members and others in reviewing the activities of the plan for the year. They do not reflect the funding requirements of the plan or the benefit security of individual participants.

The majority of plan investments are held in pooled investment funds administered by Alberta Treasury. Pooled investment funds have a market-based unit value that is used to allocate income to participants and to value purchases and sales of pool units.

The plan's respective percentage ownership in pooled investment funds at December 31 was as follows:

| | % Ownership | |
|---|---|---|
| | 1998 | 1997 |
| Canadian Dollar Public Bond Pool | 16.1 | 16.3 |
| Canadian Pooled Equities Fund | 21.6 | 13.0 |
| Domestic Passive Equity Pooled Fund | 21.6 | 94.6 |
| External Managers Fund | 16.9 | 18.3 |
| Global Structured Equity Pooled Fund | 16.4 | 22.1 |
| Private Bond Pool | 19.0 | 16.8 |
| Private Mortgage Pool | 18.9 | 17.9 |
| Private Real Estate Pool | 17.6 | 17.8 |
| United States Pooled Equities Fund | 17.0 | 18.1 |
| US Passive Equity Pooled Fund | 16.1 | - |

(b) Valuation of Assets and Liabilities

Investments are stated at fair value. The methods used to determine the fair value of investments held either by the plan or by pooled investment funds are explained in the following paragraphs.

Short-term securities, public fixed income securities and equities are valued at the year-end closing sale price or the average of the latest bid and ask prices quoted by an independent securities valuation company.

Private fixed income securities and mortgages are valued based on the net present value of future cash flows. These cash flows are discounted using Government of Canada bond rates adjusted for a risk premium estimated by management.

Real estate investments are reported at their most recent appraised value, net of any liabilities against the real property. Real estate properties are appraised annually by qualified external real estate appraisers.

The fair values of deposits, receivables, accrued investment income and payables are estimated to approximate their book values.

(c) Actuarial Value of Net Assets Available for Benefits

To reduce the potential volatility in the plan's funded status due to the effects of market fluctuations on investments, asset values are projected to increase at the rate of return assumed in the actuarial valuation. The actuarial value of assets is determined by averaging actual and projected asset values over three years.

(d) Income Recognition

Dividends are accrued on the ex-dividend date. Income from other investments is accrued as earned. Gains or losses on investments are recognized concurrently with changes in fair value.

(e) Foreign Exchange

Foreign currency transactions are translated into Canadian dollars using average rates of exchange, except for hedged foreign currency transactions which are translated at rates of exchange established by the terms of the forward exchange contracts. At the year-end, the fair value of investments and any other assets and liabilities denominated in a foreign currency are translated at the year-end exchange rate. Exchange differences are included in the determination of investment income.

(f) Derivative Financial Instruments

Income and expense on index swaps and interest rate swaps are accrued as earned and included in investment income. Gains and losses on forward foreign exchange contracts are recognized concurrently with changes in fair value.

Note 3 Investments (Schedules A to D)

Investments are summarized as follows:

| | 1998 | | 1997 | |
|---|---|---|---|---|
| | ($ thousands) | % | ($ thousands) | % |
| Deposit in the Consolidated Cash Investment Trust Fund (a) | $ 173,556 | 4.8 | $ 63,287 | 1.9 |
| Fixed Income Securities | | | | |
| Canadian Dollar Public Bond Pool (Schedule A) | 1,332,104 | 37.0 | 1,143,690 | 34.3 |
| Private Mortgage Pool (b) | 175,259 | 4.9 | 140,688 | 4.2 |
| Real Rate of Return Bonds (c ) | 22,753 | 0.6 | 54,844 | 1.7 |
| Private Bond Pool | 307 | - | 72,010 | 2.2 |
| Total deposits and fixed income securities (g) | 1,703,979 | 47.3 | 1,474,519 | 44.3 |
| Canadian Equities | | | | |
| Canadian Pooled Equities Fund (Schedule B) | 380,307 | 10.6 | 476,257 | 14.3 |
| Domestic Passive Equity Pooled Fund (Schedule C) | 410,354 | 11.3 | 446,648 | 13.4 |
| External Managers Fund (Canadian) (Schedule D) | 191,288 | 5.3 | 82,717 | 2.5 |
| Public, direct | 73 | - | | - |
| Structured Note | - | - | 73,947 | 2.2 |
| | 982,022 | 27.2 | 1,079,569 | 32.4 |
| Foreign Equities | | | | |
| External Managers Fund (Global) (Schedule D) | 400,542 | 11.1 | 323,772 | 9.7 |
| Global Structured Equity Pooled Fund (d) | 221,718 | 6.2 | 184,012 | 5.5 |
| US Passive Equity Pooled Fund (e) | 97,957 | 2.7 | - | - |
| External Managers Fund (United States) (Schedule D) | 96,638 | 2.7 | 71,332 | 2.2 |
| United States Pooled Equities Fund | 2,727 | 0.1 | 117,666 | 3.5 |
| | 819,582 | 22.8 | 696,782 | 20.9 |
| Equities in Real Estate | | | | |
| Private Real Estate Pool (f) | 98,122 | 2.7 | 80,823 | 2.4 |
| Total equities (g) | 1,899,726 | 52.7 | 1,857,174 | 55.7 |
| Total investments | $ 3,603,705 | 100.0 | $ 3,331,693 | 100.0 |

(a) The Consolidated Cash Investment Trust Fund is managed with the objective of providing competitive interest income to depositors while maintaining maximum security and liquidity of depositors' capital. The portfolio is comprised of high quality short-term and mid-term fixed income securities with a maximum term to maturity of five years.

(b) The Private Mortgage Pool is managed with the objective of providing investment returns higher than attainable from the publicly traded bond market over the long term. The portfolio is comprised primarily of high-quality commercial mortgage loans. In order to reduce risk, the pool only invests in loans insured by a federal agency and first-mortgage loans that provide diversification by property usage. The pool does not invest in mortgages on single family houses, hotels, motels, trailer parks or recreational properties. As at December 31, 1998, mortgages held by the pool have an average effective yield of 6.92% per annum based on market (1997: 7.64%). Approximately 90% of the mortgages held will mature within ten years (1997: 91%).

(c) Bonds are issued or guaranteed by the Government of Canada, bear interest at a fixed rate adjusted for inflation and have terms to maturity of over 20 years.

(d) The Global Structured Equity Pooled Fund is managed with the objective of providing investment returns comparable to the total return of the Morgan Stanley Capital International World Index. The pooled fund provides exposure to global markets through the use of structured investments such as foreign equity index swaps and interest rate swaps. All payments and receipts relating to swaps are in Canadian dollars. Participation in the pooled fund qualifies as a Canadian investment under the *Income Tax Act*.

(e) The US Passive Equity Pooled Fund is managed with the objective of attaining investment returns comparable to Standard & Poor's (S & P) 500 Total Return Index over a four-year period. The portfolio is comprised of publicly traded equities in the United States similar in weights to the S & P 500 Index. To enhance investment returns with no substantial increase in risks, the pooled fund also invests in futures, swaps and other structured investments.

(f) The Private Real Estate Pool is managed with the objective of providing investment returns comparable to the Russell Canadian Property Index over the long term. Real estate is held through intermediate companies, which have issued to the pool common shares and participating debentures secured by a charge on real estate. Risk is reduced by investing in properties that provide diversification by geographic location, by property type and by tenancy. As real estate returns are positively correlated to inflation and negatively correlated to returns from fixed income securities and equities, the pool provides diversification from the securities market.

(g) Fixed-income securities in the form of deposits are, for investment management purposes, treated as equity securities in as much as they are used as underlying security to support the index swaps issued directly by the plan (see Note 5). Treating direct index swaps, which amounted to $73,745,000 at December 31, 1998 (1997: $nil), as equity securities for investment management purposes results in an asset mix percentage of 45.2% deposit and fixed-income securities and 54.8% equities.

Note 4 Investment Risk Management

Actuarial liabilities of the plan are primarily affected by the long-term real rate of return on investments. Fair values of investments are exposed to credit risk and price risk. Credit risk relates to the possibility that a loss may occur from the failure of another party to perform according to the terms of a contract. Price risk is comprised of currency risk, interest rate risk and market risk. Currency risk relates to the possibility that the investments will change in value due to future fluctuations in foreign exchange rates. Interest rate risk relates to the possibility that the investments will change in value due to future fluctuations in market interest rates. Market risk relates to the possibility that the investments will change in value due to future fluctuations in market prices.

In order to earn the best possible return at an acceptable level of risk, the board has established a policy asset mix of 40% to 50% fixed income instruments and 50% to 60% equities. Investment risk is reduced through asset class diversification, diversification within each asset class, quality constraints on fixed income instruments and restrictions on amounts exposed to countries designated as emerging markets. Borrowing or leveraging is not allowed with the exception of pre-existing mortgages on real estate properties. Controls are in place respecting the use of derivatives (see Note 5). Forward foreign exchange contracts are used to manage currency exposure in connection with securities purchased in foreign currency (see Note 5).

Note 5 Index Swaps, Interest Rate Swaps and Foreign Exchange Contracts

Pooled funds use index and interest rate swaps to enhance return and for hedging risks. A swap is a contractual agreement between two parties to exchange a series of cash flows based on a notional amount and does not involve the exchange of the underlying principal. An index swap involves the exchange of a floating interest rate cash flow for one based on the performance of a market index. For interest rate swaps, parties generally exchange fixed and floating rate interest cash flows based on a notional value. There are underlying securities supporting all swaps. Leveraging is not allowed.

The following is a summary of the plan's proportionate share of the notional value of index and interest rate swaps held or issued by pooled funds at December 31, 1998.

| | 1998 | 1997 |
|---|---|---|
| | ($ thousands) | |
| Index swaps | | |
| Foreign equities | | |
| Global Structured Equity Pooled Fund | $ 206,913 | $ 144,904 |
| US Passive Equity Pooled Fund | 97,989 | - |
| Canadian equities | | |
| Domestic Passive Equity Pooled Fund | 166,596 | 232,717 |
| Direct | 73,745 | - |
| Bonds - Canadian Dollar Public Bond Pool | 243,839 | 157,457 |
| Interest Rate Swaps | | |
| Fixed to floating rates | | |
| Canadian Dollar Public Bond Pool | 163,408 | 64,681 |
| Domestic Passive Equity Pooled Fund | 113,671 | 127,280 |
| Global Structured Equity Pooled Fund | 138,332 | 123,572 |
| US Passive Equity Pooled Fund | 9,121 | - |
| | $ 1,213,614 | $ 850,611 |

Fair values of swaps have been included in the determination of the fair values of the respective pooled investment funds. Credit exposure relating to swaps is minimal as management deals only with counter-parties rated not less than AA.

Foreign exchange contracts are contractual agreements to exchange specified currencies at an agreed upon exchange rate and on an agreed settlement date in the future. As at December 31, 1998, the plan's proportionate share of outstanding forward foreign exchange contracts issued by the External Managers Fund amounted to $77,388,000 (1997: $66,608,000).

Note 6 Accounts Receivable

| | 1998 | 1997 |
|---|---|---|
| | ($ thousands) | |
| Accrued investment income | $ 1,505 | $ 1,273 |
| Receivable from Province of Alberta | - | 180 |
| Contributions Receivable | | |
| Employers | 4,770 | 3,876 |
| Employees | 4,719 | 3,887 |
| Province of Alberta | 1,388 | 1,028 |
| | $ 12,382 | $ 10,244 |

Note 7 Liability for Accrued Benefits

(a) Actuarial Valuation

An actuarial valuation of the plan was carried out as at December 31, 1998 by Buck Consultants Limited. The December 31, 1998 valuation resulted in an actuarial surplus of $406 million as disclosed in the Statement of Net Assets Available for Benefits and Liability for Accrued Benefits.

The valuation as at December 31, 1998 was determined using the projected benefit method, based on service. The assumptions used in the valuation were developed as the best estimate of expected short-term and long-term market conditions and other future events. This estimate was, after consultation with the plan's actuary, adopted by the Public Service Pension Board.

The major assumptions used were:

| | December 31 | |
|---|---|---|
| | 1998 Valuation | 1997 Valuation |
| | % | % |
| Investment return | 7.5 | 7.5 |
| Inflation rate (after phasing-in) | 3.25 | 3.5 |
| Salary escalation rate | 3.75* | 4.0* |
| Pension cost of living increase as a percentage of Alberta Consumer Price Index | 60 | 60 |

* Total rate plus merit and promotion

In accordance with the requirements of the *Public Sector Pension Plans Act*, a separate accounting is required of the pension liability with respect to service that was recognized as pensionable as at December 31, 1991. This information is provided in the Statement of Changes in Liability for Accrued Benefits which shows the principal components of the changes in the actuarial value of accrued benefits between the last two actuarial valuations.

The following table summarizes the actuarial value of net assets, liability for accrued benefits and the resulting actuarial surplus at December 31, 1998. In accordance with the provisions of the *Public Sector Pension Plans Act*, the Province of Alberta has no further liability in respect of the plan's pre-1992 unfunded liability from December 31, 1998 since the actuarial valuation as at that date shows that its unfunded liability for service prior to January 1, 1992 has been eliminated.

| | 1998 | | | 1997 |
|---|---|---|---|---|
| | Pre 1992 | Post-1991 | Total | Total |
| | ($ thousands) | | | |
| Fair value of net assets | $ 2,366,445 | $ 1,248,000 | $ 3,614,445 | $ 3,340,809 |
| Actuarial asset fluctuation reserve | (62,000) | (25,000) | (87,000) | (191,000) |
| Actuarial value of net assets | 2,304,445 | 1,223,000 | 3,527,445 | 3,149,809 |
| Liability for accrued benefits | 2,228,600 | 892,400 | 3,121,000 | 2,979,000 |
| Actuarial surplus | $ 75,845 | $ 330,600 | $ 406,445 | $ 170,809 |

(b) Sensitivity of Changes in Major Assumptions

The plan's future experience will inevitably differ, perhaps significantly, from these assumptions. Any differences between the actuarial assumptions and future experience will emerge as gains or losses in future valuations and will affect the financial position of the Plan.As at December 31, 1998, holding the nominal investment return and salary escalation assumptions constant, a 1% increase in the assumed long-term inflation rate would result in an increase in the liability for accrued benefits by approximately $140 million.

As at December 31, 1998, holding the inflation and nominal investment return assumptions constant, a 1% increase in the assumed salary escalation would result in an increase in the liability for accrued benefits by approximately $130 million.

As at December 31, 1998, holding the inflation and salary escalation assumptions constant, a 1% decrease in the assumed real long-term investment return would result in an increase in the liability for accrued benefits by approximately $462 million.

Note 8 Investment Income

| | 1998 | | | 1997 |
|---|---|---|---|---|
| | Income (a) | Change in Fair Value | Total | Total |
| | ($ thousands) | | | |
| Deposits and Fixed Income Securities: | | | | |
| Deposit in the Consolidated Cash Investment Trust Fund | $ 4,452 | $ - | $ 4,452 | $ 2,885 |
| Short-term Securities | 47 | - | 47 | 681 |
| Canadian Dollar Public Bond Pool | 78,202 | 25,918 | 104,120 | 96,674 |
| Private Mortgage Pool | 13,750 | 2,288 | 16,038 | 10,689 |
| Real Rate of Return Bonds | 2,523 | 1,993 | 4,516 | 2,566 |
| Private Bond Pool | 7,927 | (387) | 7,540 | 3,473 |
| | 106,901 | 29,812 | 136,713 | 116,968 |
| Equities: | | | | |
| Canadian Pooled Equities Fund | 10,238 | (16,705) | (6,467) | 60,179 |
| Domestic Passive Equity Pooled Fund | 23,741 | (26,900) | (3,159) | 57,188 |
| External Managers Fund (Canadian) | 904 | (9,950) | (9,046) | 15,272 |
| Structured Note | - | (1,191) | (1,191) | 11,156 |
| Canadian Swaps and Equities | 776 | 73 | 849 | (114) |
| Domestic Structured Equity Pooled Fund | - | - | - | 1,409 |
| External Managers Fund (Global) | 5,584 | 79,593 | 85,177 | 20,963 |
| Global Structured Equity Pooled Fund | 37,232 | 474 | 37,706 | 33,067 |
| US Passive Equity Pooled Fund | 15,175 | 6,442 | 21,617 | - |
| External Managers Fund (United States) | 599 | 27,734 | 28,333 | 22,753 |
| United States Pooled Equities Fund | 6 | (4,296) | (4,290) | 33,166 |
| Private Real Estate Pool | 4,488 | 6,622 | 11,110 | 13,813 |
| | 98,743 | 61,896 | 160,639 | 268,852 |
| | $ 205,644 | $ 91,708 | $ 297,352 | $ 385,820 |

(a) Income is comprised of dividends, interest and rental income.

Note 9 Administration Expenses

| | 1998 | 1997 |
|---|---|---|
| | ($ thousands) | |
| General administration costs | $ 3,214 | $ 2,329 |
| Board costs | 68 | 36 |
| Investment management costs | 557 | 451 |
| Actuarial fees | 135 | 62 |
| Other professional fees | 29 | 27 |
| | $ 4,003 | $ 2,905 |

General administration costs and board costs were paid to Alberta Pensions Administration Corporation on a cost-recovery basis.

Investment management costs were paid to Alberta Treasury and do not include custodial and external management fees, which have been deducted in arriving at investment income.

In 1998, total administration expenses of $4,003,000 amounted to $67 per member (1997: $49 per member).

Note 10 Uncertainty Due to the Year 2000

The year 2000 issue is the result of some computer systems using two digits rather than four to define the applicable year. Computer systems that have date sensitive software may recognize a date using "00" as the year 1900 rather than the year 2000, which could result in miscalculations or system failures. In addition, similar problems may arise in some systems if certain dates in 1999 are not recognized as a valid date or are recognized to represent something other than a date. The effects of the year 2000 issue may be experienced before, on, or after January 1, 2000. If not addressed, the effect on operations and financial reporting may range from minor errors to significant systems failure that could affect the ability to conduct some operations. Despite efforts to address this issue, it is not possible to be certain that all aspects of the year 2000 issue affecting the plan, including those related to the efforts of customers, suppliers and other third parties, will be fully resolved.

Note 11 Responsibility for Financial Statements

These financial statements were approved by the Public Service Pension Board.

Schedule A

## PUBLIC SERVICE PENSION PLAN
## SCHEDULE OF INVESTMENTS IN CANADIAN DOLLAR PUBLIC BOND POOL (a) (b)
## DECEMBER 31, 1998

($ thousands)

| | 1998 | | 1997 | |
|---|---|---|---|---|
| | Plan's Share | Total Pool | Plan's Share | Total Pool |
| Deposit in the Consolidated Cash Investment Trust Fund | $ 7,559 | $ 46,902 | $ 15,578 | $ 95,277 |
| Public Fixed Income Securities | | | | |
| Government of Canada, direct and guaranteed | 430,935 | 2,673,774 | 450,217 | 2,753,641 |
| Provincial: | | | | |
| Alberta, direct and guaranteed | 31,549 | 195,750 | 42,425 | 259,481 |
| Other, direct and guaranteed | 186,571 | 1,157,596 | 180,354 | 1,103,095 |
| Municipal | 10,358 | 64,266 | 14,245 | 87,124 |
| Corporate | 469,244 | 2,911,470 | 429,010 | 2,623,937 |
| Private Fixed Income Securities | | | | |
| Corporate | 183,343 | 1,137,571 | - | - |
| Total deposit and fixed income securities | 1,319,559 | 8,187,329 | 1,131,829 | 6,922,555 |
| Receivable from sale of investments and accrued investment income | 17,918 | 111,173 | 14,292 | 87,414 |
| Liabilities for investment purchases | (5,373) | (33,341) | (2,431) | (14,868) |
| | 12,545 | 77,832 | 11,861 | 72,546 |
| | $ 1,332,104 | $ 8,265,161 | $ 1,143,690 | $ 6,995,101 |

(a) The Canadian Dollar Public Bond Pool is managed with the objective of providing competitive returns comparable to the total return of the Scotia Capital Markets Universe Bond Index over a four-year period while maintaining adequate security and liquidity of participants' capital. The portfolio is comprised of high quality Canadian fixed income instruments and debt related derivatives. Competitive returns are achieved through management of the portfolio duration and sector rotation.

(b) Fixed income securities had an average effective current yield of 5.44% per annum based on market value (1997: 5.53% per annum). The following term structure of these securities as at December 31, 1998 is based on par value.

| | 1998 | 1997 |
|---|---|---|
| | % | |
| under 1 year | 11 | 6 |
| 1 to 5 years | 36 | 40 |
| 5 to 10 years | 26 | 23 |
| 10 to 20 years | 18 | 16 |
| over 20 years | 9 | 15 |
| | 100 | 100 |

Schedule B

# PUBLIC SERVICE PENSION PLAN
## SCHEDULE OF INVESTMENTS IN CANADIAN POOLED EQUITIES FUND (a)
## DECEMBER 31, 1998

($ thousands)

| | 1998 | | 1997 | |
|---|---|---|---|---|
| | Plan's Share | Total Pool | Plan's Share | Total Pool |
| Deposit in the Consolidated Cash Investment Trust Fund | $ 1,579 | $ 7,321 | $ 18,315 | $ 141,051 |
| Canadian Public Equities (b): | | | | |
| Common shares and rights: | | | | |
| Communications and media | 13,834 | 64,115 | 14,237 | 109,648 |
| Conglomerates | 18,154 | 84,138 | 21,995 | 169,396 |
| Consumer products | 26,326 | 122,014 | 16,908 | 130,222 |
| Financial services | 88,303 | 409,265 | 98,004 | 754,796 |
| Gold and precious minerals | 17,433 | 80,800 | 17,569 | 135,308 |
| Industrial products | 69,550 | 322,345 | 78,692 | 606,054 |
| Merchandising | 8,456 | 39,192 | 14,570 | 112,209 |
| Metals and minerals | 15,348 | 71,135 | 24,563 | 189,175 |
| Oil and gas | 31,959 | 148,122 | 76,285 | 587,518 |
| Paper and forest products | 8,250 | 38,238 | 13,655 | 105,164 |
| Pipelines | 10,781 | 49,968 | 10,125 | 77,978 |
| Real estate and construction | 8,957 | 41,512 | 8,008 | 61,673 |
| Transportation and environmental services | 13,377 | 61,998 | 20,547 | 158,248 |
| Utilities | 44,755 | 207,427 | 39,498 | 304,198 |
| Passive index | 1,869 | 8,663 | 1,856 | 14,291 |
| Options and other | - | - | 148 | 1,137 |
| | 377,352 | 1,748,932 | 456,660 | 3,517,015 |
| Receivable from sale of investments and accrued investment income | 5,186 | 24,034 | 2,391 | 18,413 |
| Liabilities for investment purchases | (3,810) | (17,657) | (1,109) | (8,544) |
| | 1,376 | 6,377 | 1,282 | 9,869 |
| | $ 380,307 | $ 1,762,630 | $ 476,257 | $ 3,667,935 |

(a) The Canadian Pooled Equities Fund is managed with the objective of providing returns higher than the total return of the Toronto Stock Exchange 300 index over a four-year period while maintaining preservation of participants' capital. The portfolio is comprised of publicly traded equities in Canadian corporations. Risk is reduced by prudent security selection and sector rotation.

(b) The industrial classifications are those used by the Toronto Stock Exchange.

Schedule C

## PUBLIC SERVICE PENSION PLAN
## SCHEDULE OF INVESTMENTS IN DOMESTIC PASSIVE EQUITY POOLED FUND (a)
## DECEMBER 31, 1998
($ thousands)

| | 1998 | | 1997 | |
|---|---|---|---|---|
| | Plan's Share | Total Pool | Plan's Share | Total Pool |
| Deposit in the Consolidated Cash Investment Trust Fund | $ 7,451 | $ 34,407 | $ 2,956 | $ 3,124 |
| Short-term Securities | 2,799 | 12,924 | 4,683 | 4,950 |
| Floating Rate Note Pool | 126,230 | 582,896 | 103,657 | 109,554 |
| Fixed Income Securities | | | | |
| Corporate | - | - | 12,563 | 13,278 |
| | 136,480 | 630,227 | 123,859 | 130,906 |
| Canadian Public Equities (b): | | | | |
| Common shares and rights: | | | | |
| Communications and media | 12,817 | 59,184 | 10,664 | 11,271 |
| Conglomerates | 8,438 | 38,966 | 7,342 | 7,760 |
| Consumer products | 17,166 | 79,267 | 10,224 | 10,806 |
| Financial services | 50,525 | 233,311 | 37,881 | 40,036 |
| Gold and precious minerals | 12,768 | 58,961 | 10,838 | 11,454 |
| Industrial products | 45,543 | 210,306 | 37,374 | 39,500 |
| Merchandising | 9,395 | 43,386 | 10,155 | 10,732 |
| Metals and minerals | 8,187 | 37,807 | 8,231 | 8,699 |
| Oil and gas | 21,927 | 101,252 | 29,692 | 31,381 |
| Paper and forest products | 6,320 | 29,186 | 6,462 | 6,829 |
| Pipelines | 7,337 | 33,881 | 4,782 | 5,054 |
| Real estate and construction | 5,471 | 25,262 | 4,342 | 4,589 |
| Transportation and environmental services | 5,787 | 26,723 | 6,890 | 7,282 |
| Utilities | 29,488 | 136,165 | 18,902 | 19,977 |
| | 241,169 | 1,113,657 | 203,779 | 215,370 |
| Domestic Structured Equity Pooled Fund | 26,277 | 121,340 | 115,548 | 122,121 |
| Passive index | - | - | 4,814 | 5,088 |
| | 267,446 | 1,234,997 | 324,141 | 342,579 |
| United States Public Equities | 549 | 2,535 | - | - |
| Receivable from sale of investments and accrued investment income | 7,911 | 36,530 | 751 | 794 |
| Liabilities for investment purchases | (2,032) | (9,383) | (2,103) | (2,223) |
| | 5,879 | 27,147 | (1,352) | (1,429) |
| | $ 410,354 | $ 1,894,906 | $ 446,648 | $ 472,056 |

(a) The Domestic Passive Equity Pooled Fund is managed on a passive approach with the objective of providing investment returns comparable to the Toronto Stock Exchange (TSE) 300 Index. The portfolio is comprised of publicly traded equities in Canadian corporations similar in weights to the TSE 300 Index. To enhance investment returns with no substantial increase in risks, the pooled fund invests in the Domestic Structured Equity Pooled Fund (DSEP) and the Floating Rate Note Pool (FRNP) which are pooled investment funds administered by Alberta Treasury. DSEP replicates the TSE 100 Index with index-based securities and structured investments such as index swaps and interest rate swaps. It provides returns comparable to the TSE 100 index. FRNP is managed with the objective of providing a reinvestment vehicle for participants with structured investments in equities and bonds. Through the use of structured investments such as interest rate swaps, FRNP provides investment opportunities in high quality floating rate instruments with remaining term-to-maturity of ten years or less.

(b) The industrial classifications are those used by the Toronto Stock Exchange.

# PUBLIC SERVICE PENSION PLAN
## SCHEDULE OF INVESTMENTS IN EXTERNAL MANAGERS FUND (a) (b)
## DECEMBER 31, 1998

($ thousands)

| | 1998 | | 1997 | |
|---|---|---|---|---|
| | Plan's Share | Total Pool | Plan's Share | Total Pool |
| Foreign Public Equity Pools | | | | |
| Multi Region | $ 182,262 | $ 1,069,544 | $ 200,438 | $ 1,109,831 |
| Europe | 134,925 | 835,531 | 55,680 | 308,298 |
| Pacific Basin | 75,327 | 457,418 | 67,654 | 374,599 |
| Emerging markets | 8,028 | 47,107 | - | - |
| | 400,542 | 2,409,600 | 323,772 | 1,792,728 |
| United States | 96,638 | 597,487 | 71,332 | 394,964 |
| Canadian Public Equity Pools | | | | |
| Large Cap | 120,199 | 646,679 | - | - |
| Small Cap | 71,089 | 428,952 | 82,717 | 425,762 |
| | 191,288 | 1,075,631 | 82,717 | 425,762 |
| | $ 688,468 | $ 4,082,718 | $ 477,821 | $ 2,613,454 |

(a) The fund is managed by external managers with expertise in global and Canadian equity markets. The objective of the fund is to provide investment returns higher than the total return of the applicable Morgan Stanley Capital International, Standard & Poor and Toronto Stock Exchange indices over a four-year period. The portfolio is comprised of publicly traded equity securities on Canadian and approved foreign markets. Risk is reduced through manager, style and market diversification.

(b) The following is a summary of assets and liabilities of the External Managers Fund as at December 31, 1998:

| | 1998 | 1997 |
|---|---|---|
| | ($ thousands) | |
| Cash and short-term securities | $ 189,924 | $ 140,359 |
| Receivables from sale of investments and accrued investment income | 18,071 | 27,024 |
| Investments | | |
| Public equities | 3,914,560 | 2,468,879 |
| Convertible bonds | 1,173 | 3,583 |
| Liability for investment purchases | (41,010) | (26,391) |
| | $ 4,082,718 | $ 2,613,454 |

SPECIAL FORCES PENSION PLAN
FINANCIAL STATEMENTS
DECEMBER 31, 1998



## AUDITOR'S REPORT

To the Special Forces Pension Board

I have audited the statement of net assets available for benefits and accrued benefits of the Special Forces Pension Plan as at December 31, 1998 and the statement of changes in net assets available for benefits for the year then ended, and the statements of changes in accrued benefits and changes in deficiency for the three years then ended. These financial statements are the responsibility of the Plan's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In my opinion, these financial statements present fairly, in all material respects, the financial position of the Plan as at December 31, 1998 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles.

Peter Valentine, FCA
Auditor General

Edmonton, Alberta
June 21, 1999

## SPECIAL FORCES PENSION PLAN
## STATEMENT OF NET ASSETS AVAILABLE FOR BENEFITS AND ACCRUED BENEFITS
## AS AT DECEMBER 31, 1998

($ thousands)

| | 1998 | 1997 |
|---|---|---|
| **NET ASSETS AVAILABLE FOR BENEFITS** | | |
| Assets | | |
| Investments (Note 3) | $ 841,830 | $ 784,319 |
| Accounts receivable (Note 6) | 364 | 422 |
| | 842,194 | 784,741 |
| Liabilities | | |
| Accounts payable (Note 7) | 167 | 31 |
| Net assets available for benefits | 842,027 | 784,710 |
| Actuarial asset fluctuation reserve (Note 8) | 35,000 | 58,000 |
| Actuarial value of net assets available for benefits | $ 807,027 | $ 726,710 |
| **ACCRUED BENEFITS** | | |
| Actuarial value of accrued benefits (Note 9) | | |
| Plan Fund | $ 826,100 | $ 712,000 |
| Indexing Fund (Note 17) | 12,191 | 32,426 |
| | $ 838,291 | $ 744,426 |
| Excess of actuarial value of accrued benefits over actuarial value of net assets (Note 9) | | |
| Plan Fund * | $ (31,264) | $ (17,716) |
| Indexing Fund (Note 17) | - | - |
| | $ (31,264) | $ (17,716) |

* The excess of actuarial value of accrued benefits over actuarial value of Plan Fund net assets is comprised of a pre-1992 deficiency of $51,164,000 (1997: $36,100,000) and a post-1991 surplus of $19,900,000 (1997: $18,384,000).

*See accompanying notes and schedules*

## SPECIAL FORCES PENSION PLAN
## STATEMENT OF CHANGES IN NET ASSETS AVAILABLE FOR BENEFITS
## FOR THE YEAR ENDED DECEMBER 31, 1998

($ thousands)

| | Plan Fund | Indexing Fund | 1998 | 1997 |
|---|---|---|---|---|
| Increase in assets | | | | |
| Investment income (Note 10) | $ 60,449 | $ 2,705 | $ 63,154 | $ 88,060 |
| Contributions (Note 11) | 25,697 | 2,060 | 27,757 | 26,483 |
| Total increase in assets before transfer | 86,146 | 4,765 | 90,911 | 114,543 |
| Decrease in assets | | | | |
| Pension benefits | 32,564 | - | 32,564 | 29,755 |
| Refunds to members | 489 | - | 489 | 259 |
| Administration expenses (Note 12) | 541 | - | 541 | 404 |
| Total decrease in assets before transfer | 33,594 | - | 33,594 | 30,418 |
| Increase in net assets before transfer | 52,552 | 4,765 | 57,317 | 84,125 |
| Transfer from the Indexing Fund to the Plan Fund (Note 13) | 25,000 | (25,000) | - | - |
| Increase (decrease) in net assets for the year | 77,552 | (20,235) | 57,317 | 84,125 |
| Net assets available for benefits at beginning of year | 752,284 | 32,426 | 784,710 | 700,585 |
| Net assets available for benefits at end of year | $ 829,836 | $ 12,191 | $ 842,027 | $ 784,710 |

*See accompanying notes and schedules.*

## SPECIAL FORCES PENSION PLAN
## STATEMENT OF CHANGES IN ACCRUED BENEFITS
## FOR PERIODS ENDED DECEMBER 31

($ thousands)

| | Three Years Ended December 31, 1998 | | | Two Years Ended December 31, 1995 |
|---|---|---|---|---|
| | Pre-1992 | Post-1991 | Total | |
| Increase in accrued benefits | | | | |
| Interest accrued on benefits | $ 143,300 | $ 25,000 | $ 168,300 | $ 113,500 |
| Cost-of-living indexing adjustments and interest | - | 32,591 | 32,591 | - |
| Benefits earned | | 60,100 | 60,100 | 40,400 |
| Experience losses (gains) | 34,500 | 8,600 | 43,100 | (65,600) |
| Changes in actuarial assumptions | 4,800 | 2,500 | 7,300 | (9,800) |
| Increase in accrued benefits | 182,600 | 128,791 | 311,391 | 78,500 |
| Decrease in accrued benefits | | | | |
| Benefits, transfers and interest | 93,700 | 6,300 | 100,000 | 44,600 |
| Net increase in accrued benefits | 88,900 | 122,491 | 211,391 | 33,900 |
| Accrued benefits at beginning of period | 551,300 | 75,600 | 626,900 | 593,000 |
| Accrued benefits at end of period (Note 9) | $ 640,200 | $ 198,091 | $ 838,291 | $ 626,900 |

*See accompanying notes and schedules.*

# SPECIAL FORCES PENSION PLAN
# STATEMENT OF CHANGES IN DEFICIENCY
# FOR PERIODS ENDED DECEMBER 31

($ thousands)

| | Three Years Ended December 31, 1998 | | | Two Years Ended December 31, |
|---|---|---|---|---|
| | Pre-1992 | Post-1991 | Total | 1995 |
| Surplus (Deficiency) at beginning of period as originally reported | $ (71,542) | $ 28,581 | $ (42,961) | $ (124,916) |
| Actuarial asset fluctuation reserve (Note 8) | (5,982) | (838) | (6,820) | - |
| Surplus (Deficiency) at beginning of period as restated | (77,524) | 27,743 | (49,781) | (124,916) |
| Net increase in net assets available for benefits | 123,560 | 118,648 | 242,208 | 91,422 |
| Net decrease (increase) in actuarial asset fluctuation reserve | (8,300) | (4,000) | (12,300) | 24,433 |
| Net increase in accrued benefits | (88,900) | (122,491) | (211,391) | (33,900) |
| Surplus (Deficiency) at end of period | $ (51,164) | $ 19,900 | $ (31,264) | $ (42,961) |

*See accompanying notes and schedules.*

## SPECIAL FORCES PENSION PLAN
## NOTES TO THE FINANCIAL STATEMENTS
## DECEMBER 31, 1998

Note 1 Summary Description of the Plan

The following description of the Special Forces Pension Plan is a summary only. For a complete description of the plan, reference should be made to the *Public Sector Pension Plans Act*, Chapter P-30.7, Statutes of Alberta 1993 and Alberta Regulation 369/93.

(a) General

The Special Forces Pension Plan is a contributory defined benefit pension plan for police officers employed by participating local authorities in Alberta.

(b) Funding

Plan Fund

Current service costs are funded by employers and employees at rates which are expected to provide for all benefits payable under the plan. The rates in effect at December 31, 1998, are 8.30 percent of pensionable salary for employers and 7.20 percent for employees. Rates are to be reviewed at least once every three years by the Special Forces Pension Board based on recommendations of the plan's actuary.

The unfunded liability for service prior to December 31, 1991 as determined by actuarial valuation is being financed by additional contributions from the Province of Alberta, employers and employees. Additional contributions are payable until December 31, 2036 unless the unfunded liability has been previously eliminated. The rates in effect at December 31, 1998 are 1.25 percent of pensionable salary for the Province of Alberta, and 0.75 percent each for employers and employees.

Indexing Fund

Benefit payments are funded by post-1991 cost-of-living adjustment (COLA) (see Note 1(i)) contributions from employers and employees at rates that are expected to meet or exceed the funding or solvency requirements of the plan. The rates in effect at December 31, 1998 are 0.75 percent of pensionable salary each for employers and employees. Rates are to be reviewed at least once every three years by the board based on recommendations of the plan's actuary.

Subject to the *Employment Pension Plans Act*, the indexing fund may receive surpluses of the plan fund respecting service after 1991.

(c) Retirement Benefits

The plan provides for a pension of 2.0 percent for each year of pensionable service based on the average salary of the five highest consecutive years. The maximum service allowable under the plan is 35 years. Members are entitled to a pension if they have at least 25 years of service or have at least five years of service and attained age 55. Pensions will be reduced at the age of 65.

(d) Disability Benefits

Pensions are payable to members who become totally disabled and retire early with at least five years of service. Reduced pensions are payable to members who become partially disabled and retire early with at least five years of service.

(e) Death Benefits

Death benefits are payable on the death of a member if the member had at least five years of service. Benefits may take the form of a survivor pension, if the beneficiary is a spouse or a dependent minor child, or a lump sum payment. A surviving spouse or the beneficiary of a deceased member with less than five years of service is entitled to receive death benefits in the form of a lump sum payment.

(f) Termination Benefits

Members who terminate with at least five years of service and who are not immediately entitled to a pension may receive a refund of contributions and interest on service prior to 1992 and the commuted value for service after 1991, subject to lock-in provisions. Alternatively, they may elect to receive a deferred pension. Members who terminate with less than five years of service receive a refund of contributions and interest.

(g) Guarantee

Payment of all benefits arising from service before 1994, excluding post-1991 COLA benefits on 1992 and 1993 service (see Note 1 (i)), is guaranteed by the Province of Alberta.

(h) Prior Service and Transfers

All prior service purchases are to be made on a basis that is cost-neutral to the plan.

All existing reciprocal agreements were terminated in 1994. New reciprocal agreements have been or are in the process of being renegotiated to provide that transferred-in service be on an actuarial reserve basis and transfers-out receive the greater of the termination benefits or commuted value for all service.

(i) Cost-of-Living Adjustments (COLA)

Pensions payable by the plan fund are increased each year by 60 percent of the increase in the Alberta Consumer Price Index for service before 1992. Cost-of-living adjustments for service after 1991 are payable by the indexing fund at rates determined by the Special Forces Pension Board.

(j) Income Taxes

The plan is a registered pension plan as defined in the *Income Tax Act* and is not subject to income taxes. The plan's registration number is 0584375.

Note 2 Summary of Significant Accounting Policies and Reporting Practices

(a) Basis of Presentation

These financial statements are prepared on the going concern basis in accordance with generally accepted accounting principles. The statements provide information about the net assets available in the plan to meet future benefit payments and are prepared to assist plan members and others in reviewing the activities of the plan for the year. They do not reflect the funding requirements of the plan or the benefit security of individual participants.

The majority of plan investments are held in pooled investment funds administered by Alberta Treasury. Pooled investment funds have a market-based unit value that is used to allocate income to participants and to value purchases and sales of pool units.

The plan's respective percentage ownership in pooled investment funds at December 31, 1998 was as follows:

| | % Ownership | |
|---|---|---|
| | 1998 | 1997 |
| Canadian Dollar Public Bond Pool | 3.4 | 3.5 |
| Canadian Pooled Equities Fund | 6.6 | 6.5 |
| Domestic Passive Equity Pooled Fund | 5.0 | - |
| Domestic Structured Equity Pooled Fund | 0.4 | 0.4 |
| External Managers Fund | 4.5 | 4.7 |
| Global Structured Equity Pooled Fund | 2.5 | 3.4 |
| Private Bond Pool | 4.1 | 4.9 |
| Private Equity Pool | 6.3 | 5.6 |
| Private Mortgage Pool | 4.1 | 3.5 |
| Private Real Estate Pool | 4.0 | 4.0 |
| Transition Account | 7.4 | - |
| United States Pooled Equities Fund | 4.5 | 4.7 |
| US Passive Equity Pooled Fund | 4.3 | - |

(b) Valuation of Assets and Liabilities

Investments are stated at fair value. The methods used to determine the fair value of investments held either by the plan or by pooled investment funds are explained in the following paragraphs.

Short-term securities, public fixed income securities and equities are valued at the year-end closing sale price or the average of the latest bid and ask prices quoted by an independent securities valuation company.

Private fixed income securities and mortgages are valued based on the net present value of future cash flows. These cash flows are discounted using Government of Canada bond rates adjusted for a risk premium estimated by management.

The fair value of private equities is estimated by management.

Real estate investments are reported at their most recent appraised value, net of any liabilities against the real property. Real estate properties are appraised annually by qualified external real estate appraisers.

The fair values of deposits, receivables, accrued investment income and payables are estimated to approximate their book values.

(c) Actuarial Value of Net Assets Available for Benefits

To moderate the effects of market volatility on investment value, annual net realized and unrealized gains and losses are amortized equally over three years.

(d) Income Recognition

Dividends are accrued on the ex-dividend date. Income from other investments is accrued as earned. Gains or losses on investments are recognized concurrently with changes in fair value.

(e) Foreign Exchange

Foreign currency transactions are translated into Canadian dollars using average rates of exchange, except for hedged foreign currency transactions which are translated at rates of exchange established by the terms of the forward exchange contracts. At year-end, the fair value of investments and any other assets and liabilities denominated in a foreign currency are translated at the year-end exchange rate. Exchange differences are included in the determination of investment income.

(f) Derivative Financial Instruments

Income and expense on index swaps and interest rate swaps are accrued as earned and included in investment income. Gains and losses on forward foreign exchange contracts are recognized concurrently with changes in fair value.

Note 3 Investments (Schedules A to D)

Investments are summarized as follows:

| | 1998 | | 1997 | |
|---|---|---|---|---|
| | ($ thousands) | % | ($ thousands) | % |
| Deposit in the Consolidated Cash Investment Trust Fund (a) | $ 8,197 | 1.0 | $ 2,118 | 0.3 |
| Fixed Income Securities | | | | |
| Canadian Dollar Public Bond Pool (Schedule A) | 278,745 | 33.1 | 246,790 | 31.4 |
| Private Mortgage Pool (b) | 37,886 | 4.5 | 27,774 | 3.5 |
| Real Rate of Return Bonds (c) | 3,226 | 0.4 | 13,288 | 1.7 |
| Private Bond Pool | 66 | - | 20,970 | 2.7 |
| Total deposits and fixed income securities | 328,120 | 39.0 | 310,940 | 39.6 |
| Canadian Equities | | | | |
| Canadian Pooled Equities Fund (Schedule B) | 117,337 | 13.9 | 237,522 | 30.3 |
| Transition Account and miscellaneous | 91 | - | - | - |
| Domestic Passive Equity Pooled Fund (Schedule C) | 95,249 | 11.3 | - | - |
| Domestic Structured Equity Pooled Fund (d) | 493 | 0.1 | 496 | 0.1 |
| External Managers Fund (Canadian) (Schedule D) | 52,537 | 6.2 | 19,184 | 2.4 |
| Private Equity Pool (e) | 6,057 | 0.7 | 6,735 | 0.9 |
| Structured Note (f) | 27,596 | 3.3 | 28,112 | 3.6 |
| Foreign Equities | | | | |
| External Managers Fund (Global) (Schedule D) | 105,363 | 12.5 | 84,875 | 10.8 |
| Global Structured Equity Pooled Fund (g) | 34,505 | 4.1 | 28,637 | 3.7 |
| US Passive Equity Pooled Fund (h) | 25,863 | 3.1 | - | - |
| External Managers Fund (United States) (Schedule D) | 25,520 | 3.0 | 18,699 | 2.4 |
| United States Pooled Equities Fund | 715 | 0.1 | 30,844 | 3.9 |
| Equities in Real Estate | | | | |
| Private Real Estate Pool (i) | 22,384 | 2.7 | 18,275 | 2.3 |
| Total equities | 513,710 | 61.0 | 473,379 | 60.4 |
| Total investments | $ 841,830 | 100.0 | $ 784,319 | 100.0 |

(a) The Consolidated Cash Investment Trust Fund is managed with the objective of providing competitive interest income to depositors while maintaining maximum security and liquidity of depositors' capital. The portfolio is comprised of high quality short-term and mid-term fixed income securities with a maximum term to maturity of five years.

(b) The Private Mortgage Pool is managed with the objective of providing investment returns higher than attainable from the publicly traded bond market over the long term. The portfolio is comprised primarily of high-quality commercial mortgage loans. In order to reduce risk, the pool only invests in loans insured by a federal agency and first-mortgage loans that provide diversification by property usage. The pool does not invest in mortgages on single family houses, hotels, motels, trailer parks or recreational properties. As at December 31, 1998, mortgages held by the pool have an average effective yield of 6.92% per annum based on market (1997: 7.64% per annum). Approximately 90% of the mortgages held will mature within ten years (1997: 91%).

(c) Real rate of return bonds are issued or guaranteed by the Government of Canada, bear interest at a fixed rate adjusted for inflation, and have terms to maturity of over 20 years.

(d) The Domestic Structured Equity Pooled Fund is passively managed with the objective of providing investment returns equal to the total return of the Toronto Stock Exchange (TSE) 100 index at costs lower than actively managed domestic equity pools. The pooled fund replicates the TSE 100 Index with index-based securities and structured investments such as index swaps and interest rate swaps.

(e) The Private Equity Pool is managed with the objective of providing investment returns higher than attainable from publicly traded equity indices such as the Toronto Stock Exchange 300 Index over the long term. The portfolio is comprised of equity investments in companies that show higher than average growth potential. Risk is reduced by avoiding direct investments in start-up and venture capital situations and by limiting holdings in any single company.

(f) The structured note ranks equally with all deposit liabilities of a chartered bank, matures in February 1999 and attracts yields equalling 100% of the upside of the Toronto Stock Exchange 100 Index.

(g) The Global Structured Equity Pooled Fund is managed with the objective of providing investment returns comparable to the total return of the Morgan Stanley Capital International World Index. The pooled fund provides exposure to global markets through the use of structured investments such as foreign equity index swaps and interest rate swaps. All payments and receipts relating to swaps are in Canadian dollars. Participation in the pooled fund qualifies as a Canadian investment under the Income Tax Act.

(h) The US Passive Equity Pooled Fund is managed with the objective of attaining investment returns comparable to Standard & Poor's (S & P) 500 Total Return Index over a four-year period. The portfolio is comprised of publicly traded equities in the United States similar in weights to the S & P 500 Index. To enhance investment returns with no substantial increase in risks, the pooled fund also invests in futures, swaps and other structured investments.

(i) The Private Real Estate Pool is managed with the objective of providing investment returns comparable to the Russell Canadian Property Index over the long term. Real estate is held through intermediate companies, which have issued to the pool common shares and participating debentures secured by a charge on real estate. Risk is reduced by investing in properties that provide diversification by geographic location, by property type and by tenancy. As real estate returns are positively correlated to inflation and negatively correlated to returns from fixed income securities and equities, the pool provides diversification from the securities market.

Note 4 Investment Risk Management

Fair values of investments are exposed to credit risk and price risk. Credit risk relates to the possibility that a loss may occur from the failure of another party to perform according to the terms of a contract. Price risk is comprised of currency risk, interest rate risk and market risk. Currency risk relates to the possibility that the investments will change in value due to future fluctuations in foreign exchange rates. Interest rate risk relates to the possibility that the investments will change in value due to future fluctuations in market interest rates. Market risk relates to the possibility that the investments will change in value due to future fluctuations in market prices.

Actuarial liabilities of the plan are primarily affected by the long-term real rate of return on investments. In order to earn the best possible return at an acceptable level of risk, the board has established a policy asset mix of 30% to 60% fixed income instruments and 40% to 70% equities. Investment risk is reduced through asset class diversification, diversification within each asset class, quality constraints on fixed income instruments, and restrictions on amounts exposed to countries designated as emerging markets. Borrowing or leveraging is not allowed with the exception of pre-existing mortgages on real estate properties. Controls are in place respecting the use of derivatives (see Note 5). Forward foreign exchange contracts are used to manage currency exposure in connection with securities purchased in foreign currency (see Note 5).

Note 5 Index Swaps, Interest Rate Swaps and Foreign Exchange Contracts

Pooled funds use index and interest rate swaps to enhance return and for hedging risks. A swap is a contractual agreement between two parties to exchange a series of cash flows based on a notional amount and does not involve the exchange of the underlying principal. An index swap involves the exchange of a floating interest rate cash flow for one based on the performance of a market index. For interest rate swaps, parties generally exchange fixed and floating rate interest cash flows based on a notional value. There are underlying securities supporting all swaps. Leveraging is not allowed.

The following is a summary of the plan's proportionate share of the notional value of index and interest rate swaps held or issued by pooled funds at December 31, 1998.

| | 1998 | 1997 |
|---|---|---|
| | ($ thousands) | |
| Index Swaps | | |
| Foreign equities | | |
| Global Structured Equity Pooled Fund | $ 32,201 | $ 22,551 |
| US Passive Equity Pooled Fund | 25,872 | - |
| Canadian equities | | |
| Domestic Passive Equity Pooled Fund | 38,669 | - |
| Domestic Structured Equity Pooled Fund | 477 | 482 |
| Bonds - Canadian Dollar Public Bond Pool | 51,024 | 33,977 |
| Interest Rate Swaps | | |
| Fixed to floating rates | | |
| Canadian Dollar Public Bond Pool | 34,193 | 13,957 |
| Domestic Passive Equity Pooled Fund | 26,385 | - |
| Domestic Structured Equity Pooled Fund | 303 | 149 |
| Global Structured Equity Pooled Fund | 21,528 | 19,231 |
| US Passive Equity Pooled Fund | 2,408 | - |
| | $ 233,060 | $ 90,347 |

Foreign exchange contracts are contractual agreements to exchange specified currencies at an agreed upon exchange rate and on an agreed settlement date in the future. As at December 31, 1998, the plan's proportionate share of outstanding forward foreign exchange contracts issued by the External Managers Fund amounted to $20,347,000 (1997: $17,561,000).

Note 6 Accounts Receivable

| | 1998 | 1997 |
|---|---|---|
| | ($ thousands) | |
| Accrued investment income | $ 104 | $ 222 |
| Contributions Receivable | | |
| Employers | 33 | 23 |
| Employees | 30 | 22 |
| Province of Alberta | 197 | 155 |
| | $ 364 | $ 422 |

Note 7 Accounts Payable

| | 1998 | 1997 |
|---|---|---|
| | ($ thousands) | |
| Administration expenses | $ 162 | $ 18 |
| Benefits | 5 | 13 |
| | $ 167 | $ 31 |

Note 8 Change in Actuarial Value of Net Assets Available for Benefits

Investments held by the plan are stated at fair value as at December 31, 1998. In order to minimize contribution instability and the effects of market volatility on asset values, the actuarial value of assets has been determined by adjusting assets by an actuarial asset fluctuation reserve. The method of determining the actuarial value of net assets available for benefits has been changed from that used in 1995, 1996 and 1997 on the recommendations of the plan's actuary. Prior to 1998, the adjustment was determined by amortizing annual net unrealized gains and losses equally over three years. In 1998, the adjustment was determined by amortizing annual net realized and unrealized gains and losses equally over three years to reduce fluctuations due to timing and frequency of asset transactions. As with the accrued pension liability, the actuarial asset fluctuation reserve has been allocated between the pre-1992 and post-1991 periods.

The actuarial asset fluctuation reserve for 1995 and 1997 has been restated to reflect this change in accounting method. The change in method has the effect of reducing the actuarial value of net assets available for benefits and increasing the deficiency by $23.8 million in 1998 (1997: $32.8 million). If the change had not been made, the deficiency of the plan would have been $7.5 million as at December 31, 1998 (1997: surplus $23.3 million).

Note 9 Accrued Benefits

(a) Actuarial Valuation

An actuarial valuation of the plan was carried out as at December 31, 1998 by William M. Mercer Limited. The December 31, 1998 valuation resulted in a deficiency of $31.3 million as disclosed in the Statement of Net Assets Available for Benefits and Accrued Benefits.

The valuation as at December 31, 1998 was determined using the projected benefit method prorated on service. The assumptions used in the valuation were developed as the best estimate of expected short-term and long-term market conditions and other future events. This estimate was, after consultation with the plan's actuary, adopted by the Special Forces Pension Board.

The major assumptions used were:

| | December 31 | |
|---|---|---|
| | 1998 Valuation | 1995 Valuation |
| | % | % |
| Investment return | 7.5 | 8.0 |
| Inflation rate (after phasing-in) | 3.5 | 4.0 |
| Salary escalation rate (after phasing-in)* | 4.0 | 4.5 |
| Pension cost-of-living increase as a percent of Alberta Consumer Price Index for pre 1996 service only | 60 | 60 |

* Disclosed rate plus merit and promotion

In accordance with the requirements of the *Public Sector Pension Plans Act*, a separate accounting is required of the pension liability with respect to service that was recognized as pensionable as at December 31, 1991. This information is provided in the Statement of Changes in Accrued Benefits, which shows the principal components of the change in the actuarial value of accrued benefits between the last two actuarial valuations.

Based on the information provided above, the following table summarizes the actuarial value of net assets, accrued benefits, and the resulting deficiency of the Plan Fund as at December 31, 1998.

| | 1998 | | | 1997 |
|---|---|---|---|---|
| | Pre-1992 | Post-1991 | Total | Total |
| | ($ thousands) | | | |
| Plan Fund net assets available for benefits | $616,836 | $213,000 | $829,836 | $752,284 |
| Actuarial asset fluctuation reserve (Note 8) | 27,800 | 7,200 | 35,000 | 58,000 |
| Plan Fund actuarial value of net assets | 589,036 | 205,800 | 794,836 | 694,284 |
| Plan Fund accrued benefits | 640,200 | 185,900 | 826,100 | 712,000 |
| Plan Fund surplus (deficiency) | $ (51,164) | $ 19,900 | $ (31,264) | $ (17,716) |

As at December 31, 1998, the Indexing Fund held investments of $12,191,000 (1997 $32,426,000) with offsetting accrued benefits of the same amount.

(b) Sensitivity of Changes in Major Assumptions

The plan's future experience will inevitably differ, perhaps significantly, from the assumptions. Any differences between the actuarial assumptions and future experience will emerge as gains or losses in future valuations and will affect the financial position of the plan.

As at December 31, 1998, holding the nominal investment return and salary escalation assumptions constant, a 1% increase in the assumed long-term inflation rate would result in an increase in accrued benefits of the plan fund by approximately $55.3 million.

As at December 31, 1998, holding the inflation and nominal investment return assumptions constant, a 1% increase in the assumed salary escalation would result in an increase in accrued benefits of the plan fund by approximately $26.9 million.

As at December 31, 1998, holding the inflation and salary escalation assumptions constant, a 1% increase in the assumed real long-term investment return would result in a decrease in accrued benefits of the plan fund by approximately $99.6 million.

Note 10 Investment Income

| | 1998 | | | 1997 |
|---|---|---|---|---|
| | Income (a) | Change in Fair Value | Total | Total |
| | ($ thousands) | | | |
| Deposits and Fixed Income Securities: | | | | |
| Deposit in the Consolidated Cash Investment Trust Fund | $ 282 | $ - | $ 282 | $ 370 |
| Canadian Dollar Public Bond Pool | 16,798 | 5,304 | 22,102 | 22,203 |
| Private Mortgage Pool | 2,820 | 344 | 3,164 | 2,127 |
| Real Rate of Return Bonds | 620 | 364 | 984 | 615 |
| Private Bond Pool | 1,719 | 16 | 1,735 | 948 |
| | 22,239 | 6,028 | 28,267 | 26,263 |
| Equities: | | | | |
| Canadian Pooled Equities Fund | 2,858 | (7,128) | (4,270) | 27,648 |
| Transition Account and miscellaneous | 2,124 | 11,338 | 13,462 | - |
| Domestic Passive Equity Pooled Fund | (4,164) | (12,918) | (17,082) | - |
| Domestic Structured Equity Pooled Fund | (6) | 3 | (3) | (4) |
| External Managers Fund (Canadian) | 298 | 329 | 627 | 3,534 |
| Canadian Public Equities | - | (516) | (516) | 4,132 |
| Private Equity Pool | 113 | (177) | (64) | 502 |
| External Managers Fund (Global) | 1,464 | 20,879 | 22,343 | 4,531 |
| Global Structured Equity Pooled Fund | 5,794 | 74 | 5,868 | 5,115 |
| US Passive Equity Pooled Fund | 4,005 | 1,675 | 5,680 | - |
| External Managers Fund (United States) | 157 | 7,282 | 7,439 | 5,513 |
| United States Pooled Equities Fund | 2 | (1,129) | (1,127) | 7,696 |
| Private Real Estate Pool | 1,024 | 1,506 | 2,530 | 3,130 |
| | 13,669 | 21,218 | 34,887 | 61,797 |
| | $ 35,908 | $ 27,246 | $ 63,154 | $ 88,060 |

(a) Income is comprised of dividends, interest and rental income.

Note 11 Contributions

| | 1998 | 1997 |
|---|---|---|
| | ($ thousands) | |
| Current and past service | | |
| Employers | $ 12,528 | $ 11,644 |
| Employees | 11,424 | 10,645 |
| Unfunded liability | | |
| Employers | 1,030 | 998 |
| Employees | 1,030 | 998 |
| Province of Alberta | 1,716 | 1,663 |
| Transfers from other plans | 29 | 535 |
| | $ 27,757 | $ 26,483 |

Note 12 Administration Expenses

| | 1998 | 1997 |
|---|---|---|
| | ($ thousands) | |
| General administration costs | $ 333 | $ 280 |
| Investment management costs | 170 | 114 |
| Actuarial fees | 38 | 10 |
| | $ 541 | $ 404 |

General administration costs including plan board costs were paid to Alberta Pensions Administration Corporation on a cost-recovery basis.

Investment management costs were paid to Alberta Treasury and do not include custodial and external management fees, which have been deducted in arriving at investment income.

Total administration expenses amounted to $146 per member (1997: $ 116 per member). The $30 per member cost increase in 1998 is attributed to the following factors: changes in the accounting treatment of business process reengineering cost $12, increase in investment management cost $13, and increase in operating and plan specific cost $5.

Note 13 Transfer from the Indexing Fund to the Plan Fund

Transfer from the Indexing Fund to the Plan Fund is determined by the plan's actuary to finance the payment of cost-of-living increases by the Plan Fund for pensionable service after 1991 [see Note 1(i)].

Note 14 Remuneration of Board Members

Remuneration paid to board members, as approved by the Lieutenant Governor in Council, is as follows:

| | Chairman | Members (6) |
|---|---|---|
| Daily Remuneration Rate | | |
| Up to 4 hours | $ 135 | $ 100 |
| 4 to 8 hours | 230 | 165 |
| Over 8 hours | 365 | 260 |
| During 1998, the following amounts were paid: | | |
| Remuneration | $ 2,375 | $ 11,078 |
| Travel expenses | 1,747 | 12,626 |

Remuneration with respect to the board member nominated by the Government of Alberta belongs to the Crown, and is to be paid to the Provincial Treasurer.

Note 15 Budget Information

The accrued benefits are based on the Special Forces Pension Board's best estimates of future events after consultation with the plan's actuary. Differences between actual results and management's expectations are disclosed as net experience gains and losses in the statement of changes in accrued benefits. Accordingly, a budget is not included in these financial statements.

Note 16 Uncertainty Due to the Year 2000

The year 2000 issue is the result of some computer systems being written using two digits rather than four to define the applicable year. Computer systems that have date sensitive software may recognize a date using "00" as the year 1900 rather than the year 2000, which could result in miscalculations or system failures. In addition, similar problems may arise in some systems if certain dates in 1999 are not recognized as a valid date or are recognized to represent something other than a date. The effects of the year 2000 issue may be experienced before, on, or after January 1, 2000. If not addressed, the effect on operations and financial reporting may range from minor errors to significant systems failure that could affect the ability to conduct some operations. Despite efforts to address this issue, it is not possible to be certain that all aspects of the year 2000 issue affecting the plan, including those related to the efforts of customers, suppliers and other third parties, will be fully resolved.

Note 17 Restatement of Comparative Figures

Actuarial value of accrued benefits of the Indexing Fund, as previously reported, totalling $24,200,000 has been increased by $8,226,000 to reflect liabilities of the Indexing Fund respecting post 1995 service. The restatement has the effect of increasing the excess of actuarial value of accrued benefits over actuarial value of net assets by $8,226,000.

Comparative figures have been restated to be consistent with the 1998 presentation.

Note 18 Responsibility for Financial Statements

These financial statements were prepared by management and approved by the Special Forces Pension Board.

# SPECIAL FORCES PENSION PLAN
## SCHEDULE OF INVESTMENTS IN CANADIAN DOLLAR PUBLIC BOND POOL (a) (b)
## DECEMBER 31, 1998

($ thousands)

| | 1998 | | 1997 | |
|---|---|---|---|---|
| | Plan's Share | Total Pool | Plan's Share | Total Pool |
| Deposit in the Consolidated Cash Investment Trust Fund | $ 1,582 | $ 46,902 | $ 3,361 | $ 95,277 |
| Public Fixed Income Securities | | | | |
| Government of Canada, direct and guaranteed | 90,174 | 2,673,774 | 97,149 | 2,753,641 |
| Provincial: | | | | |
| Alberta, direct and guaranteed | 6,602 | 195,750 | 9,155 | 259,481 |
| Other, direct and guaranteed | 39,040 | 1,157,596 | 38,918 | 1,103,095 |
| Municipal | 2,167 | 64,266 | 3,074 | 87,124 |
| Corporate | 98,190 | 2,911,470 | 92,574 | 2,623,937 |
| Private Fixed Income Securities | | | | |
| Corporate | 38,366 | 1,137,571 | - | - |
| Total deposit and fixed income securities | 276,121 | 8,187,329 | 244,231 | 6,922,555 |
| Receivable from sale of investments and accrued investment income | 3,749 | 111,173 | 3,084 | 87,414 |
| Liabilities for investment purchases | (1,125) | (33,341) | (525) | (14,868) |
| | 2,624 | 77,832 | 2,559 | 72,546 |
| | $ 278,745 | $ 8,265,161 | $ 246,790 | $ 6,995,101 |

(a) The Canadian Dollar Public Bond Pool is managed with the objective of providing competitive returns comparable to the total return of the Scotia Capital Markets Universe Bond Index over a four-year period while maintaining adequate security and liquidity of participants' capital. The portfolio is comprised of high quality Canadian fixed income instruments and debt related derivatives. Competitive returns are achieved through management of portfolio duration and sector rotation.

(b) Fixed income securities had an average effective current yield of 5.44% per annum based on market value (1997: 5.53% per annum). The following term structure of these securities as at December 31, 1998 is based on par value.

| | 1998 | 1997 |
|---|---|---|
| | % | |
| under 1 year | 11 | 6 |
| 1 to 5 years | 36 | 40 |
| 5 to 10 years | 26 | 23 |
| 10 to 20 years | 18 | 16 |
| over 20 years | 9 | 15 |
| | 100 | 100 |

Schedule B

# SPECIAL FORCES PENSION PLAN
## SCHEDULE OF INVESTMENTS IN CANADIAN POOLED EQUITIES FUND (a)
## DECEMBER 31, 1998

($ thousands)

| | 1998 | | 1997 | |
|---|---|---|---|---|
| | Plan's Share | Total Pool | Plan's Share | Total Pool |
| Deposit in the Consolidated Cash Investment Trust Fund | $ 487 | $ 7,321 | $ 9,134 | $ 141,051 |
| Canadian Public Equities (b): | | | | |
| Common shares and rights: | | | | |
| Communications and media | 4,268 | 64,115 | 7,100 | 109,648 |
| Conglomerates | 5,601 | 84,138 | 10,969 | 169,396 |
| Consumer products | 8,122 | 122,014 | 8,433 | 130,222 |
| Financial services | 27,244 | 409,265 | 48,878 | 754,796 |
| Gold and precious minerals | 5,379 | 80,800 | 8,762 | 135,308 |
| Industrial products | 21,458 | 322,345 | 39,246 | 606,054 |
| Merchandising | 2,609 | 39,192 | 7,266 | 112,209 |
| Metals and minerals | 4,736 | 71,135 | 12,250 | 189,175 |
| Oil and gas | 9,860 | 148,122 | 38,045 | 587,518 |
| Paper and forest products | 2,545 | 38,238 | 6,810 | 105,164 |
| Pipelines | 3,326 | 49,968 | 5,050 | 77,978 |
| Real estate and construction | 2,764 | 41,512 | 3,994 | 61,673 |
| Transportation and environmental services | 4,127 | 61,998 | 10,248 | 158,248 |
| Utilities | 13,809 | 207,427 | 19,699 | 304,198 |
| Passive index | 577 | 8,663 | 925 | 14,291 |
| Options and other | - | - | 74 | 1,137 |
| | 116,425 | 1,748,932 | 227,749 | 3,517,015 |
| Receivable from sale of investments and accrued investment income | 1,600 | 24,034 | 1,192 | 18,413 |
| Liabilities for investment purchases | (1,175) | (17,657) | (553) | (8,544) |
| | 425 | 6,377 | 639 | 9,869 |
| | $ 117,337 | $ 1,762,630 | $ 237,522 | $ 3,667,935 |

(a) The Canadian Pooled Equities Fund (CPE) is managed with the objective of providing returns higher than the Toronto Stock Exchange 300 Index while maintaining preservation of participants' capital. The portfolio is comprised of publicly traded equities in the Canadian market. Risk is reduced by prudent security selection and sector rotation. During the year, a portion of the plan's investments held by the CPE was transferred to the Domestic Passive Equity Pooled Fund through the Transition Account.

(b) The industrial classifications are those used by the Toronto Stock Exchange.

Schedule C

# SPECIAL FORCES PENSION PLAN
## SCHEDULE OF INVESTMENTS IN DOMESTIC PASSIVE EQUITY POOLED FUND (a)
## DECEMBER 31, 1998
($ thousands)

| | Plan's Share | Total Pool |
|---|---|---|
| Deposit in the Consolidated Cash Investment Trust Fund | $ 1,730 | $ 34,407 |
| Short-term Securities | 650 | 12,924 |
| Floating Rate Note Pool | 29,300 | 582,896 |
| | 31,680 | 630,227 |
| Canadian Public Equities (b): | | |
| Common shares and rights: | | |
| Communications and media | 2,975 | 59,184 |
| Conglomerates | 1,958 | 38,966 |
| Consumer products | 3,984 | 79,267 |
| Financial services | 11,728 | 233,311 |
| Gold and precious minerals | 2,963 | 58,961 |
| Industrial products | 10,572 | 210,306 |
| Merchandising | 2,180 | 43,386 |
| Metals and minerals | 1,900 | 37,807 |
| Oil and gas | 5,090 | 101,252 |
| Paper and forest products | 1,467 | 29,186 |
| Pipelines | 1,703 | 33,881 |
| Real estate and construction | 1,270 | 25,262 |
| Transportation and environmental services | 1,343 | 26,723 |
| Utilities | 6,845 | 136,165 |
| | 55,978 | 1,113,657 |
| Domestic Structured Equity Pooled Fund | 6,099 | 121,340 |
| United States Public Equities | 127 | 2,535 |
| Receivable from sale of investments and accrued investment income | 1,837 | 36,530 |
| Liabilities for investment purchases | (472) | (9,383) |
| | 1,365 | 27,147 |
| | $ 95,249 | $ 1,894,906 |

(a) The Domestic Passive Equity Pooled Fund is managed on a passive approach with the objective of providing investment returns comparable to the Toronto Stock Exchange (TSE) 300 Index. The portfolio is comprised of publicly traded equities in Canadian corporations similar in weights to the TSE 300 Index. To enhance investment returns with no substantial increase in risks, the pooled fund invests in the Domestic Structured Equity Pooled Fund (DSEP) and the Floating Rate Note Pool (FRNP) which are pooled investment funds administered by Alberta Treasury. DSEP replicates the TSE 100 Index with index-based securities and structured investments such as index swaps and interest rate swaps. It provides returns comparable to the TSE 100 index. FRNP is managed with the objective of providing a reinvestment vehicle for participants with structured investments in equities and bonds. Through the use of structured investments such as interest rate swaps, FRNP provides investment opportunities in high quality floating rate instruments with remaining term-to-maturity of ten years or less.

(b) The industrial classifications are those used by the Toronto Stock Exchange.

# SPECIAL FORCES PENSION PLAN
# SCHEDULE OF INVESTMENTS IN EXTERNAL MANAGERS FUND
# DECEMBER 31, 1998

($ thousands)

| | 1998 | | 1997 | |
|---|---|---|---|---|
| | Plan's Share | Total Pool | Plan's Share | Total Pool |
| Foreign Public Equity Pools | | | | |
| Multi Region | $ 47,779 | $ 1,069,544 | $ 52,545 | $ 1,109,831 |
| Europe | 35,639 | 835,531 | 14,595 | 308,298 |
| Pacific Basin | 19,841 | 457,418 | 17,735 | 374,599 |
| Emerging Markets | 2,104 | 47,107 | - | - |
| | 105,363 | 2,409,600 | 84,875 | 1,792,728 |
| United States | 25,520 | 597,487 | 18,699 | 394,964 |
| Canadian Public Equity Pools | | | | |
| Large Cap | 36,050 | 646,679 | - | - |
| Small Cap | 16,487 | 428,952 | 19,184 | 425,762 |
| | 52,537 | 1,075,631 | 19,184 | 425,762 |
| | $ 183,420 | $ 4,082,718 | $ 122,758 | $ 2,613,454 |

(a) The fund is managed by external managers with expertise in global and Canadian equity markets. The objective of the fund is to provide investment returns higher than the total return of the applicable Morgan Stanley Capital International, Standard & Poor and Toronto Stock Exchange indices over a four-year period. The portfolio is comprised of publicly traded equity securities on Canadian and approved foreign markets. Risk is reduced through manager, style and market diversification.

(b) The following is a summary of assets and liabilities of the External Managers Fund as at December 31, 1998.

| | 1998 | 1997 |
|---|---|---|
| | ($ thousands) | |
| Cash and short-term securities | $ 189,924 | $ 140,359 |
| Receivables from sale of investments and accrued investment income | 18,071 | 27,024 |
| Investments | | |
| Public equities | 3,914,560 | 2,468,879 |
| Convertible bonds | 1,173 | 3,583 |
| Liability for investment purchases | (41,010) | (26,391) |
| | $ 4,082,718 | $ 2,613,454 |

## UNIVERSITIES ACADEMIC PENSION PLAN
## FINANCIAL STATEMENTS
## DECEMBER 31, 1998



## AUDITOR'S REPORT

To the Universities Academic Pension Board

I have audited the statement of net assets and accrued pension liability of the Universities Academic Pension Plan as at December 31, 1998 and the statement of changes in net assets available for benefits for the year then ended, and the statements of changes in accrued pension liability and changes in deficiency for the two years then ended. These financial statements are the responsibility of the Plan's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In my opinion, these financial statements present fairly, in all material respects, the financial position of the Plan as at December 31, 1998 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles.

Peter Valentine, FCA
Auditor General

Edmonton, Alberta
April 30, 1999

## UNIVERSITIES ACADEMIC PENSION PLAN
## STATEMENT OF NET ASSETS
## AND ACCRUED PENSION LIABILITY
## AS AT DECEMBER 31, 1998

($ thousands)

| | 1998 | 1997 |
|---|---|---|
| Net assets available for benefits | | |
| Assets | | |
| Investments (Note 3) | $ 1,539,311 | $ 1,463,482 |
| Accrued investment income | 2,322 | 626 |
| Contributions receivable: | | |
| Employers | 1,731 | 1,686 |
| Employees | 1,866 | 1,798 |
| Province of Alberta | 287 | 286 |
| | 1,545,517 | 1,467,878 |
| Liabilities | | |
| Accounts payable and accrued liabilities | 547 | 436 |
| Net assets available for benefits | 1,544,970 | 1,467,442 |
| Actuarial asset fluctuation reserve (Note 6) | (27,300) | (83,400) |
| Actuarial value of net assets | 1,517,670 | 1,384,042 |
| Deficiency | 172,730 | 143,558 |
| Accrued pension liability | $ 1,690,400 | $ 1,527,600 |

*See accompanying notes and schedules.*

## UNIVERSITIES ACADEMIC PENSION PLAN
## STATEMENT OF CHANGES IN NET ASSETS
## AVAILABLE FOR BENEFITS
## FOR THE YEAR ENDED DECEMBER 31, 1998

($ thousands)

| | 1998 | 1997 |
|---|---|---|
| Contributions received | | |
| Current and past service: | | |
| Employers | $ 18,515 | $ 18,801 |
| Employees | 20,155 | 20,233 |
| Additional contributions to meet pre-1992 unfunded liability: | | |
| Employers | 2,404 | 2,460 |
| Employees | 2,404 | 2,460 |
| Province of Alberta | 3,435 | 3,267 |
| Transfers from other plans | 309 | 289 |
| | 47,222 | 47,510 |
| Other income | | |
| Net investment income (Note 7) | 108,802 | 164,886 |
| Payments made | | |
| Pension benefits | (73,629) | (66,532) |
| Refunds to members | (3,531) | (4,986) |
| Transfers to other plans | (402) | (24) |
| Plan expenses (Note 8) | (934) | (705) |
| | (78,496) | (72,247) |
| Increase in net assets | 77,528 | 140,149 |
| Net assets available for benefits at beginning of year | 1,467,442 | 1,327,293 |
| Net assets available for benefits at end of year | $ 1,544,970 | $ 1,467,442 |

*See accompanying notes and schedules.*

## UNIVERSITIES ACADEMIC PENSION PLAN
## STATEMENT OF CHANGES IN ACCRUED PENSION LIABILITY
## FOR PERIODS ENDED DECEMBER 31

($ thousands)

| | Two years ended December 31, 1998 | | | Two years ended December 31, 1996 |
|---|---|---|---|---|
| | Pre-1992 | Post-1991 | Total | Total |
| Increase in accrued pension liability | | | | |
| Interest accrued on liability | $ 205,500 | $ 36,400 | $ 241,900 | $ 220,830 |
| Benefits earned | - | 83,900 | 83,900 | 86,600 |
| Net experience losses (gains) | 15,500 | 11,000 | 26,500 | (28,300) |
| Changes in actuarial assumptions | 33,900 | 15,400 | 49,300 | (32,800) |
| Changes in TIAA - CREF balance | 3,200 | - | 3,200 | 1,500 |
| Present value of prior service payments due | 1,600 | (600) | 1,000 | 2,900 |
| Increase in accrued pension liability | 259,700 | 146,100 | 405,800 | 250,730 |
| Decrease in accrued pension liability | | | | |
| Benefits paid, including interest | 145,100 | 15,800 | 160,900 | 113,100 |
| Decrease in accrued pension liability | 145,100 | 15,800 | 160,900 | 113,100 |
| Net increase in accrued pension liability | 114,600 | 130,300 | 244,900 | 137,630 |
| Accrued pension liability at beginning of period | 1,228,521 | 216,979 | 1,445,500 | 1,307,870 |
| Accrued pension liability at end of period (Note 9) | $ 1,343,121 | $ 347,279 | $ 1,690,400 | $ 1,445,500 |

The periods presented coincide with the performance of the actuarial valuations carried out at December 31, 1994 and 1996, and 1998.

*See accompanying notes and schedules.*

## UNIVERSITIES ACADEMIC PENSION PLAN
## STATEMENT OF CHANGES IN DEFICIENCY
## FOR PERIODS ENDED DECEMBER 31

($ thousands)

| | Two years ended December 31, 1998 | | | Two years ended December 31, 1996 |
|---|---|---|---|---|
| | Pre-1992 | Post-1991 | Total | Total |
| Deficiency (surplus) at beginning of period as originally reported | $ 234,328 | $ (31,321) | $ 203,007 | $ 273,222 |
| Actuarial asset fluctuation reserve (Note 6) | 15,700 | 3,400 | 19,100 | - |
| Deficiency (surplus) at beginning of period as restated | 250,028 | (27,921) | 222,107 | 273,222 |
| Net increase in net assets available for benefits | (96,607) | (121,070) | (217,677) | (332,945) |
| Net increase (decrease) in actuarial asset fluctuation reserve | (64,600) | (12,000) | (76,600) | 125,100 |
| Net increase in accrued pension liability | 114,600 | 130,300 | 244,900 | 137,630 |
| Deficiency (surplus) at end of period | $ 203,421 | $ (30,691) | $ 172,730 | $ 203,007 |

*See accompanying notes and schedules.*

# UNIVERSITIES ACADEMIC PENSION PLAN
# NOTES TO THE FINANCIAL STATEMENTS
# DECEMBER 31, 1998

Note 1 Summary Description of the Plan

The following description of the Universities Academic Pension Plan is a summary only. For a complete description of the plan, reference should be made to the *Public Sector Pension Plans Act*, Chapter P-30.7, Statutes of Alberta 1993 and Alberta Regulation 370/93.

(a) General

The Universities Academic Pension Plan is a contributory defined benefit pension plan for all academic staff members and other eligible employees of the universities of Alberta, Calgary, Lethbridge, Athabasca University, and The Banff Centre.

(b) Funding Policy

Contributions under the plan and investment earnings are expected to fund all benefits payable under the plan. Contributions are reviewed in consultation with the plan's actuary at least once every three years by the Universities Academic Pension Board.

Current service costs for the universities of Alberta, Calgary and Lethbridge are funded by matching employee and employer contributions on pensionable salaries. Rates in effect at December 31, 1998, are 5.5% of pensionable salary up to the Canada Pension Plan's Year's Maximum Pensionable Earnings (YMPE) and 7.9% for any excess.

Rates in effect for employees of Athabasca University and The Banff Centre are 5.0% of pensionable salaries up to the Canada Pension Plan's YMPE and are 7.4% for any excess. Employers contribute at a rate 1.0% more than employees.

The unfunded liability for service prior to January 1, 1992 as determined by actuarial valuation is being financed by additional contributions from the Province of Alberta, employers and employees. Contribution rates are set on the basis that the additional contributions will eliminate the unfunded liability on or before December 31, 2043. The employer and employee rate at December 31, 1998 is 0.875% each of salary and the rate for the Province of Alberta is 1.25% of salary.

(c) Retirement Benefits

The plan provides for a pension of 2.0% for each year of pensionable service, based on the average salary of the highest five consecutive years. The maximum service allowable under the plan is 35 years. The plan's benefits and contributions were integrated with the Canada Pension Plan as of January 1, 1994. As a result, pensions for service after 1993 are reduced at age 65. The reduction is based on 0.6% of the Canada Pension Plan's five-year average YMPE immediately preceding termination.

Subject to certain conditions, members are entitled to an actuarial unreduced pension for service before 1994 if they have attained age 65 and have at least five years of service or have attained age 55 and have at least ten years of service.

Members are entitled to an actuarial unreduced pension for service after 1993 if they have either attained age 60 and have at least five years of service or have attained age 55 and the sum of their age and service equals 80.

Members are entitled to an actuarial reduced pension for service after 1993 if they have attained age 55 and have at least five years of service.

(d) Disability Benefits

Members who become disabled and are in receipt of benefits from an approved disability plan continue to earn pensionable service credits under the plan.

Members who become disabled and have at least five years of service and are not in receipt of benefits from an approved disability plan are eligible to apply for a disability pension. If total service is less than ten years, the pension is based on post-1993 service only. A reduced pension is paid where the member is partially disabled.

(e) Death Benefits

Death benefits are payable on the death of a member. If the member had at least ten years of service, a surviving spouse may choose to receive a survivor pension based on total service. For service between five and ten years, the surviving spouse may choose to receive a pension based on the post-1993 service and a lump sum payment for pre-1994 service. For a beneficiary other than a spouse, or where service is less than five years, a lump sum payment must be chosen.

(f) Termination Benefits

Termination benefits for service before 1994 are different than for service after 1993.

Refunds in relation to service performed before 1994 are based on both employee and employer contributions plus interest if transferred directly to a RRSP. Otherwise, refunds are restricted to employee contributions and interest.

For service after 1993, the refund depends on whether the member has more or less than five years of total service. If the member has five or more years of service, the refund is based on the greater of the commuted value or 1.75 times employee contributions and interest. If the member has less than five years service, the refund is equal to employee contributions plus interest. Refunds are subject to the plan lock-in provisions.

Members who terminate with fewer than five years of service and who are not immediately entitled to a pension may receive a refund.

Members who terminate with more than five years of service and are not immediately entitled to a pension may elect to receive a refund or a deferred pension.

(g) Prior Service and Transfers

All prior service purchases are to be made on a basis that is cost-neutral to the plan.

Reciprocal agreements provide that transferred-in service be on an actuarial reserve basis and transferred-out service receive the greater of the termination benefits or commuted value for all service.

(h) Cost-of-Living Adjustments

Pensions payable are increased each year by an amount equal to at least 60% of the increase in the Alberta Consumer Price Index.

(i) Income Taxes

The plan is a registered pension plan as defined in the *Income Tax Act*. The plan's registration number is 0339572.

Note 2 Summary of Significant Accounting Policies and Reporting Practices

(a) Basis of Presentation

These financial statements are prepared on the going concern basis in accordance with generally accepted accounting principles. The statements provide information about the net assets available in the plan to meet future benefit payments and are prepared to assist plan members and others in reviewing the activities of the plan for the year. They do not reflect the funding requirements of the plan or the benefit security of individual participants.

The majority of plan investments are held in pooled investment funds administered by Alberta Treasury. Pooled investment funds have a market-based unit value that is used to allocate income to participants and to value purchases and sales of pool units.

(b) Valuation of Assets and Liabilities

Investments are stated at fair value. The methods used to determine the fair value of investments held either by the plan or by pooled investment funds are explained in the following paragraphs.

Short-term securities, public fixed income securities and equities are valued at the year-end closing sale price or the average of the latest bid and ask prices quoted by an independent securities valuation company.

Private fixed income securities and mortgages are valued based on the net present value of future cash flows. These cash flows are discounted using Government of Canada bond rates adjusted for a risk premium estimated by management.

The fair value of private equities is estimated by management.

Real estate investments are reported at their most recent appraised value, net of any liabilities against the real property. Real estate properties are appraised annually by qualified external real estate appraisers.

The fair values of deposits, receivables, accrued investment income and payables are estimated to approximate their book values.

(c) Actuarial Value of Net Assets Available for Benefits

To reduce the potential volatility in the plan’s funded status due to the effects of market fluctuations on investments, asset values are adjusted by an actuarial asset fluctuation reserve. Assets are projected to increase at the rate of return assumed in the actuarial valuation. The actuarial value of assets is determined by averaging actual and projected asset values over three years.

(d) Income Recognition

Dividends are accrued on the ex-dividend date. Income from other investments is accrued as earned. Gains or losses on investments are recognized concurrently with changes in fair value.

(e) Foreign Exchange

Foreign currency transactions are translated into Canadian dollars using average rates of exchange, except for hedged foreign currency transactions which are translated at rates of exchange established by the terms of the forward exchange contracts. At year-end, the fair value of investments and any other assets and liabilities denominated in a foreign currency are translated at the year-end exchange rate. Exchange differences are included in the determination of investment income.

(f) Derivative Financial Instruments

Income and expense on index swaps and interest rate swaps are accrued as earned and included in investment income. Gains and losses on forward foreign exchange contracts are recognized concurrently with changes in fair value.

## Note 3 Investments (Schedules A to C)

Investments are summarized as follows as at December 31:

| | 1998 | | 1997 | |
|---|---|---|---|---|
| | ($ thousands) | % | ($ thousands) | % |
| Deposit in the Consolidated Cash | | | | |
| Investment Trust Fund (a) | $ 19,640 | 1.3 | $ 27,105 | 1.9 |
| Fixed Income Securities | | | | |
| Canadian Dollar Public Bond Pool (b) | 21,079 | 1.4 | 464,084 | 31.7 |
| Canadian Long Bond Pool (Schedule A) | 424,018 | 27.5 | - | |
| Real Rate of Return Bonds (c) | 153,105 | 9.9 | 27,836 | 1.9 |
| Private Bond Pool | 65 | - | 30,883 | 2.1 |
| Private Mortgage Pool | - | - | 58,630 | 4.0 |
| Total deposit and fixed income securities | 617,907 | 40.1 | 608,538 | 41.6 |
| Canadian Equities | | | | |
| Canadian Pooled Equities Fund (d) | 106,603 | 6.9 | 476,016 | 32.5 |
| Transition Account and miscellaneous (d) | 181 | - | - | - |
| Domestic Passive Equity Pooled Fund (Schedule B) | 218,236 | 14.2 | - | - |
| Domestic Structured Equity Pooled Fund (e) | 16,801 | 1.1 | 16,909 | 1.2 |
| External Managers Fund (Canadian) (Schedule C) | 115,860 | 7.5 | 37,020 | 2.5 |
| Private Equity Pool (f) | 9,226 | 0.6 | 12,319 | 0.8 |
| Foreign Equities | | | | |
| External Managers Fund (Global) (Schedule C) | 187,267 | 12.2 | 142,731 | 9.8 |
| Global Structured Equity Pooled Fund (g) | 134,374 | 8.7 | 53,726 | 3.7 |
| US Passive Equity Pooled Fund (h) | 48,598 | 3.2 | - | - |
| External Managers Fund (United States) (Schedule C) | 48,097 | 3.1 | 31,446 | 2.2 |
| United States Pooled Equities Fund | 1,202 | 0.1 | 51,871 | 3.5 |
| Equities in Real Estate | | | | |
| Private Real Estate Pool (i) | 34,959 | 2.3 | 32,906 | 2.2 |
| Total equities | 921,404 | 59.9 | 854,944 | 58.4 |
| Total investments | $ 1,539,311 | 100.0 | $ 1,463,482 | 100.0 |

(a) The Consolidated Cash Investment Trust Fund is managed with the objective of providing competitive interest income to depositors while maintaining maximum security and liquidity of depositors' capital. The portfolio is comprised of high-quality short-term and mid-term fixed income securities with a maximum term to maturity of five years.

(b) The Canadian Dollar Public Bond Pool is managed with the objective of providing competitive returns comparable to the total return of the Scotia Capital Markets Universe Bond Index over a four-year period while maintaining adequate security and liquidity of participants' capital. The portfolio is comprised of high quality Canadian fixed income instruments and debt related derivatives. Competitive returns are achieved through management of the portfolio duration and sector rotation. As at December 31, 1998, securities held by the Pool have an average effective yield of 5.44% per annum based on market (1997: 5.53% per annum). Approximately 73% (1997: 69%) of the securities held will mature in 10 years.

(c) Real rate of return bonds are issued or guaranteed by the Government of Canada, bear interest at a fixed rate adjusted for inflation and have terms to maturity of over 20 years.

(d) The Canadian Pooled Equities Fund (CPE) is managed with the objective of providing returns higher than the total return of the Toronto Stock Exchange 300 Index while maintaining preservation of participants' capital. The portfolio is comprised of publicly traded equities in Canadian corporations. Risk is reduced by prudent security selection and sector rotation. During the year, a portion of the plan's investments held by the CPE was transferred to the Domestic Passive Equity Pooled Fund through the Transition Account.

(e) The Domestic Structured Equity Pooled Fund is managed with the objective of providing investment returns equal to the total return of the Toronto Stock Exchange (TSE) 100 index at costs lower than actively managed domestic equity pools. The pooled fund replicates the TSE 100 Index with index-based securities and structured investments such as index swaps and interest rate swaps.

(f) The Private Equity Pool is managed with the objective of providing investment returns higher than attainable from the publicly traded equity indices such as the Toronto Stock Exchange 300 Index over the long term. The portfolio is comprised of equity investments in companies that show higher than average growth potential. Risk is reduced by avoiding direct investments in start-up and venture capital situations and by limiting holdings in any single company.

(g) The Global Structured Equity Pooled Fund is managed with the objective of providing investment returns comparable to the total return of the Morgan Stanley Capital International World Index. The pooled fund provides exposure to global markets through the use of structured investments such as foreign equity index swaps and interest rate swaps. All payments and receipts relating to swaps are in Canadian dollars. Participation in the pooled fund qualifies as a Canadian investment under the *Income Tax Act*.

(h) The US Passive Equity Pooled Fund is managed with the objective of attaining investment returns comparable to Standard & Poor's (S & P) 500 Total Return Index over a four-year period. The portfolio is comprised of publicly traded equities in the United States similar in weights to the S & P 500 Index. To enhance investment returns with no substantial increase in risks, the pooled fund also invests in futures, swaps and other structured investments.

(i) The Private Real Estate Pool is managed with the objective of providing investment returns comparable to the Russell Canadian Property Index over the long term. Real estate is held through intermediate companies, which have issued to the Pool common shares and participating debentures secured by a charge on real estate. Risk is reduced by investing in properties that provide diversification by geographic location, by property type and by tenancy. As real estate returns are positively correlated to inflation and negatively correlated to returns from fixed income securities and equities, the pool provides diversification from the securities market.

Note 4 Investment Risk Management

Investment risk is reduced through asset class diversification, diversification within each asset class, quality constraints on fixed income instruments and restrictions on amounts exposed to countries designated as emerging markets. Borrowing or leveraging is not allowed with the exception of pre-existing mortgages on real estate properties. Controls are in place respecting the use of derivatives (see Note 5). Forward foreign exchange contracts are used to manage currency exposure in connection with securities purchased in foreign currency (see Note 5).

Note 5 Index Swaps, Interest Rate Swaps and Foreign Exchange contracts

Pooled funds use index and interest rate swaps to enhance return and for hedging risk. A swap is a contractual agreement between two parties to exchange a series of cash flows based on a notional amount and does not involve the exchange of the underlying principal. An index swap involves the exchange of a floating interest rate cash flow for one based on the performance of a market index. For interest rate swaps, parties generally exchange fixed and floating rate interest cash flows based on a notional value. There are underlying securities supporting all swaps. Leveraging is not allowed.

The following is a summary of the plan's proportionate share of the notional value of index and interest rate swaps held or issued by pooled funds as at December 31, 1998:

| | 1998 | 1997 |
|---|---|---|
| | ($ thousands) | |
| Index Swaps: | | |
| Foreign equities | | |
| Global Structured Equity Pooled Fund | $ 125,401 | $ 42,308 |
| US Passive Equity Pooled Fund | 48,615 | |
| Canadian equities | | |
| Domestic Passive Equity Pooled Fund | 88,600 | - |
| Domestic Structured Equity Pooled Fund | 16,257 | 16,439 |
| Bonds - Canadian Dollar Public Bond Pool | 3,859 | 63,893 |
| Interest Rate Swaps: | | |
| Fixed to floating rates | | |
| Global Structured Equity Pooled Fund | 83,837 | 36,079 |
| US Passive Equity Pooled Fund | 4,525 | - |
| Domestic Passive Equity Pooled Fund | 60,453 | - |
| Domestic Structured Equity Pooled Fund | 10,316 | 5,050 |
| Canadian Dollar Public Bond Pool | 2,586 | 26,246 |
| Total | $ 444,449 | $ 190,015 |

Fair values of swaps have been included in the determination of the fair values of the respective pooled investment funds. Credit exposure relating to swaps is minimal as management deals only with counterparties rated not less than AA.

Foreign exchange contracts are contractual agreements to exchange specified currencies at an agreed upon exchange rate and on an agreed settlement date in the future. As at December 31, 1998, the plan's proportionate share of outstanding forward foreign exchange contracts issued by the External Managers Fund amounted to $35,893,000 (1997: $29,363,000).

Note 6 Change in Actuarial Value of Net Assets Available for Benefits

Investments held by the plan are stated at fair value as at December 31, 1998. In order to minimize contribution instability and the effects of market volatility on asset values, the actuarial value of assets has been determined by adjusting assets by an actuarial asset fluctuation reserve. The method of determining the actuarial value of net assets available for benefits has been changed from that used in 1996 and 1997 on the recommendations of the plan's actuary. Prior to 1998, the adjustment was determined by amortizing annual net unrealized gains and losses equally over three years. In 1998, asset values are projected to increase at the rate of return assumed in the actuarial valuation. The actuarial value of assets is determined by averaging actual and projected asset values over three years. The actuarial asset fluctuation reserve is the difference between the actuarial value of assets and actual asset value. As with the accrued pension liability, the actuarial asset fluctuation reserve has been allocated between the pre-1992 and post-1991 periods.

The actuarial asset fluctuation reserve for 1996 and 1997 has been restated to reflect this change in accounting method. The change in method has the effect of reducing the actuarial value of net assets available for benefits and increasing the deficiency by $16.9 million in 1998 (1997: $42.3 million). If the change had not been made, the deficiency of the plan would have been $155.8 million as at December 31, 1998 (1997: $101.3 million).

Note 7 Net Investment Income

| | 1998 Income | 1998 Change in Fair Value | 1998 Total | 1997 Total |
|---|---|---|---|---|
| | ($ thousands) | | | |
| Deposits and Fixed Income Securities: | | | | |
| Deposit in the Consolidated Cash Investment Trust Fund | $ 1,623 | $ - | $ 1,623 | $ 1,275 |
| Canadian Dollar Public Bond Pool | 24,852 | 17,937 | 42,789 | 40,809 |
| Canadian Long Bond Pool | 1,072 | (3,673) | (2,601) | - |
| Real Rate of Return Bonds | 2,243 | 826 | 3,069 | 1,260 |
| Private Bond Pool | 1,687 | 208 | 1,895 | 1,561 |
| Private Mortgage Pool | 3,026 | 886 | 3,912 | 4,325 |
| | 34,503 | 16,184 | 50,687 | 49,230 |
| Equities: | | | | |
| Canadian Pooled Equities Fund | 4,733 | (19,079) | (14,346) | 55,777 |
| Transition Account and miscellaneous [Note 3 (d)] | 4,257 | 22,722 | 26,979 | - |
| Domestic Passive Equity Pooled Fund | (7,148) | (26,127) | (33,275) | - |
| Domestic Structured Equity Pooled Fund | (194) | 86 | (108) | 1,909 |
| External Managers Fund (Canadian) | 629 | 1,258 | 1,887 | 6,837 |
| Private Equity Pool | 173 | (260) | (87) | 943 |
| External Managers Fund (Global) | 2,477 | 35,498 | 37,975 | 9,589 |
| Global Structured Equity Pooled Fund | 14,787 | (539) | 14,248 | 9,654 |
| US Passive Equity Pooled Fund | 7,472 | 2,339 | 9,811 | - |
| External Managers Fund (United States) | 273 | 12,578 | 12,851 | 10,161 |
| United States Pooled Equities Fund | 3 | (1,894) | (1,891) | 15,052 |
| Private Real Estate Pool | 1,641 | 2,430 | 4,071 | 5,734 |
| | 29,103 | 29,012 | 58,115 | 115,656 |
| | $ 63,606 | $ 45,196 | $ 108,802 | $ 164,886 |

Net investment income is comprised of dividends, interest, rental income and other non-capital returns from assets.

Note 8 Plan Expenses

| | 1998 | 1997 |
|---|---|---|
| | ($ thousands) | |
| General plan costs | $ 632 | $ 465 |
| Investment management costs | 273 | 205 |
| Actuarial fees | 29 | 35 |
| | $ 934 | $ 705 |

General plan costs including plan board costs were paid to Alberta Pensions Administration Corporation on a cost recovery basis.

Investment management costs were paid to Alberta Treasury on a cost recovery basis. External management and associated custodial fees totalling $1,050,000 (1997: $959,000), which have been deducted from investment income of the External Managers Fund, are excluded from administrative expenses of the plan.

Total expenses including external management and associated custodial fees amounted to $290 per member (1997: $252 per member). The $38 per member cost increase in 1998 is attributed to the following factors: changes in the accounting treatment of business process reengineering cost $11, increase in investment management cost $9, increase in external management cost $8, increase in general operations cost $6, and increase in plan specific cost $4.

Total expenses including external management and associated custodial fees amounted to 0.128% (1997: 0.113%) of assets under administration.

Note 9 Accrued Pension Liability

(a) Actuarial Valuation

An actuarial valuation of the plan was carried out as at December 31, 1998 by William M. Mercer Limited. The December 31, 1998 valuation resulted in a deficiency of $172.7 million as disclosed in the statement of net assets and accrued pension liability. The valuation as at December 31, 1998 was determined using the projected benefit method prorated on service. The assumptions used in the valuation were developed as the best estimate of expected short-term and long-term market conditions and other future events. After consultation with the plan's actuary, the Universities Academic Pension Board adopted this best estimate

The major assumptions used were:

| | December 31 | |
|---|---|---|
| | 1998 Valuation | 1996 Valuation |
| | % | % |
| Asset real rate of return | 4 | 4 |
| Inflation rate (after phasing-in) | 3.25 | 4 |
| Investment return | 7.25 | 8 |
| Salary escalation rate (after phasing-in) | 3.25* | 3* |
| Pension cost-of-living increase as a percentage of Alberta Consumer Price Index | 60 | 60 |

* Total rate plus merit and promotion

In accordance with the requirements of the *Public Sector Pension Plans Act*, a separate accounting is required of the pension liability with respect to service that was recognized as pensionable as at December 31, 1991. Therefore, the statement below summarizing the accrued pension liability, fair value of assets, and the resulting deficiency at December 31, 1998 is allocated between the pre-1992 and post-1991 periods:

| | Pre-1992 | Post-1991 | Total |
|---|---|---|---|
| | | ($ thousands) | |
| Fair value of assets | $ 1,160,900 | $ 384,070 | $ 1,544,970 |
| Actuarial asset fluctuation reserve | (21,200) | (6,100) | (27,300) |
| Actuarial value of net assets | 1,139,700 | 377,970 | 1,517,670 |
| Accrued pension liability | 1,343,121 | 347,279 | 1,690,400 |
| Deficiency (surplus) | $ 203,421 | $ (30,691) | $ 172,730 |

(b) Sensitivity of Changes in Major Assumptions

The plan's actual experience will inevitably differ, perhaps significantly, from these assumptions. Any differences between the actuarial assumptions and actual experience will emerge as gains or losses in future valuations and will affect the financial position of the plan.

As at December 31, 1998, holding the nominal investment return and salary escalation assumptions constant, a 1% increase in the assumed long-term inflation rate would result in an increase in the deficiency of the plan from $173 million to $256 million.

As at December 31, 1998, holding the inflation and nominal investment return assumptions constant, a 1% increase in the assumed salary escalation would result in an increase in the deficiency of the plan from $173 million to $201 million.

As at December 31, 1998, holding the inflation and salary escalation assumptions constant, a 1% increase in the assumed real long-term investment return would result in a change in the deficiency of the plan from a deficiency of $173 million to a surplus of $11 million.

Note 10 Remuneration of Board Members

Remuneration paid to board members, as approved by the Lieutenant Governor in Council, is as follows:

| | Chairman | Members (8) |
|---|---|---|
| Remuneration Rate | | |
| Up to 4 hours | $ 135 | $ 100 |
| 4 to 8 hours | 230 | 165 |
| Over 8 hours | 365 | 260 |
| During 1998, the following amounts were paid: | | |
| Remuneration | $ 4,909 | $ 31,864 |
| Travel expenses | 3,876 | 20,710 |

Remuneration with respect to the board member nominated by the Government of Alberta belongs to the Crown and is paid to the Provincial Treasurer.

Note 11 Budget Information

The accrued pension liability is based on the Universities Academic Pension Board's best estimates of future events. Differences between actual results and the board's expectations are disclosed as net experience gains or losses in the statement of changes in accrued pension liability. Accordingly, a budget is not included in these financial statements.

Note 12 Uncertainty Due to the Year 2000

The year 2000 issue is the result of some computer programs being written using two digits rather than four to define the applicable year. Computer programs that have date sensitive software may recognize a date using "00" as the year 1900 rather than the year 2000, which could result in miscalculations or system failures. In addition, similar problems may arise in some systems if certain dates in 1999 are not recognized as a valid date or are recognized to represent something other than a date. The effects of the year 2000 issue may be experienced before, on, or after January 1, 2000. If not addressed, the effect on operations and financial reporting may range from minor errors to significant systems failure that could affect the ability to conduct some operations. Despite efforts to address this issue, it is not possible to be certain that all aspects of the year 2000 issue affecting the plan, including those related to the efforts of customers, suppliers and other third parties, will be fully resolved.

Note 13 Comparative Figures

Comparative figures have been restated to be consistent with the 1998 presentation.

# UNIVERSITIES ACADEMIC PENSION PLAN
## SCHEDULE OF INVESTMENTS IN CANADIAN LONG BOND POOL (a)
## DECEMBER 31, 1998

($ thousands)

| | Plan's Share | Total Pool |
|---|---|---|
| Deposit in the Consolidated Cash | | |
| Investment Trust Fund | $ 11,139 | $ 11,139 |
| Fixed Income Securities (b) | | |
| Government of Canada | | |
| direct and guaranteed | 170,093 | 170,093 |
| Other provincial, direct and guaranteed | 127,203 | 127,203 |
| Municipal | 13,697 | 13,697 |
| Corporate | 106,725 | 106,725 |
| Total deposit and fixed income securities | 428,857 | 428,857 |
| Receivable from sale of investments | | |
| and accrued investment income | 4,935 | 4,935 |
| Liabilities for investment purchases | (9,774) | (9,774) |
| | (4,839) | (4,839) |
| | $ 424,018 | $ 424,018 |

(a) Between November 30 and December 14, 1998, the plan's share of investments held in the Canadian Dollar Public Bond Pool, the Private Bond Pool and the Private Mortgage Pool were transferred into the Canadian Long Bond Pool. The pool is managed with the objective of providing competitive returns comparable to the total return of the Scotia Capital Markets Long Bond Index over the long term while maintaining adequate security and liquidity of participants' capital. The portfolio is comprised of high quality Canadian fixed income instruments. Competitive returns are achieved through management of the portfolio duration and sector rotation.

(b) Fixed income securities had an average effective current yield of 5.52% per annum based on market value. The following term structure of these securities as at December 31, 1998 is based on par value.

| | % |
|---|---|
| 0 to 5 years | 12 |
| 5 to 10 years | 4 |
| 10 to 20 years | 21 |
| over 20 years | 63 |
| | 100 |

Schedule B

# UNIVERSITIES ACADEMIC PENSION PLAN
## SCHEDULE OF INVESTMENTS IN DOMESTIC PASSIVE EQUITY POOLED FUND (a)
## DECEMBER 31, 1998
($ thousands)

| | Plan's Share | Total Pool |
|---|---|---|
| Deposit in the Consolidated Cash | | |
| Investment Trust Fund | $ 3,963 | $ 34,407 |
| Short-term securities | 1,488 | 12,924 |
| Floating Rate Note Pool | 67,132 | 582,896 |
| | 72,583 | 630,227 |
| Canadian Public Equities (b): | | |
| Common shares and rights: | | |
| Communications and media | 6,816 | 59,184 |
| Conglomerates | 4,488 | 38,966 |
| Consumer products | 9,129 | 79,267 |
| Financial services | 26,870 | 233,311 |
| Gold and precious minerals | 6,791 | 58,961 |
| Industrial products | 24,221 | 210,306 |
| Merchandising | 4,997 | 43,386 |
| Metals and minerals | 4,354 | 37,807 |
| Oil and gas | 11,661 | 101,252 |
| Paper and forest products | 3,361 | 29,186 |
| Pipelines | 3,902 | 33,881 |
| Real estate and construction | 2,910 | 25,262 |
| Transportation and environmental services | 3,077 | 26,723 |
| Utilities | 15,682 | 136,165 |
| | 128,259 | 1,113,657 |
| Domestic Structured Equity Pooled Fund | 13,975 | 121,340 |
| United States Public Equities | 292 | 2,535 |
| Receivable from sale of investments and accrued investment income | 4,207 | 36,530 |
| Liabilities for investment purchases | (1,080) | (9,383) |
| | 3,127 | 27,147 |
| | $ 218,236 | $ 1,894,906 |

(a) The Domestic Passive Equity Pooled Fund is managed on a passive approach with the objective of providing investment returns comparable to the Toronto Stock Exchange (TSE) 300 Index. The portfolio is comprised of publicly traded equities in Canadian corporations similar in weights to the TSE 300 Index. To enhance investment returns with no substantial increase in risks, the pooled fund invests in the Domestic Structured Equity Pooled Fund (DSEP) and the Floating Rate Note Pool (FRNP) which are pooled investment funds administered by Alberta Treasury. DSEP replicates the TSE 100 Index with index-based securities and structured investments such as index swaps and interest rate swaps. It provides returns comparable to the TSE 100 index. FRNP is managed with the objective of providing a reinvestment vehicle for participants with structured investments in equities and bonds. Through the use of structured investments such as interest rate swaps, FRNP provides investment opportunities in high quality floating rate instruments with remaining term to maturity of ten years or less.

(b) The industrial classifications are those used by the Toronto Stock Exchange.

# UNIVERSITIES ACADEMIC PENSION PLAN
# SCHEDULE OF INVESTMENTS IN EXTERNAL MANAGERS FUND (a) (b)
# DECEMBER 31, 1998

($ thousands)

| | 1998 | | 1997 | |
|---|---|---|---|---|
| | Plan's Share | Total Pool | Plan's Share | Total Pool |
| Foreign Public Equity Pools | | | | |
| Multi Region | $ 80,348 | $ 1,069,544 | $ 88,361 | $ 1,109,831 |
| Europe | 67,392 | 835,531 | 24,546 | 308,298 |
| Pacific Basin | 35,988 | 457,418 | 29,824 | 374,599 |
| Emerging Markets | 3,539 | 47,107 | - | - |
| | 187,267 | 2,409,600 | 142,731 | 1,792,728 |
| United States | 48,097 | 597,487 | 31,446 | 394,964 |
| Canadian Public Equity Pools | | | | |
| Large Cap | 76,510 | 646,679 | - | - |
| Small Cap | 39,350 | 428,952 | 37,020 | 425,762 |
| | 115,860 | 1,075,631 | 37,020 | 425,762 |
| | $ 351,224 | $ 4,082,718 | $ 211,197 | $ 2,613,454 |

(a) The fund is managed by external managers with expertise in global and Canadian equity markets. The objective of the fund is to provide investment returns higher than the total return of the applicable Morgan Stanley Capital International, Standard & Poor and Toronto Stock Exchange indices over a four-year period. The portfolio is comprised of publicly traded equity securities on Canadian and approved foreign markets. Risk is reduced through manager, style and market diversification.

(b) The following is a summary of assets and liabilities of the External Managers Fund as at December 31, 1998:

| | 1998 | 1997 |
|---|---|---|
| Cash and short-term securities | $ 189,924 | $ 140,359 |
| Receivables from sale of investments and accrued investment income | 18,071 | 27,024 |
| Investments | | |
| Public equities | 3,914,560 | 2,468,879 |
| Convertible bonds | 1,173 | 3,583 |
| Liability for investment purchases | (41,010) | (26,391) |
| | $ 4,082,718 | $ 2,613,454 |

Schedule D

# UNIVERSITIES ACADEMIC PENSION PLAN
## SCHEDULE OF INVESTMENT RETURNS
## YEAR ENDED DECEMBER 31, 1998

The plan uses the time-weighted rate of return based on market values to measure performance. The measure involves the calculation of the return realized by the plan over a specified period and is a measure of the total proceeds received from an investment dollar initially invested. Total proceeds include cash distributions (interest and dividend payments) and capital gains or losses (realized and unrealized).

The time-weighted rate of return measures the compounded rate of growth of the initial investment over the specified period. It is designed to eliminate the effect that the size and timing of cash flows have on the internal rate of return. The investment industry uses time-weighted rates of return calculated using market values when comparing the returns of funds with other funds or indices.

Investment returns for the plan for the one- and five-year periods ended December 31, 1998 are as follows:

| | One Year Return | | | | | 5 Year Compound Annualized Return |
|---|---|---|---|---|---|---|
| | 1998 | 1997 | 1996 | 1995 | 1994 | |
| Time-weighted rates of return | | | | | | |
| Short-term fixed income | 5.2 | 3.6 | 6.2 | 7.2 | 4.9 | 5.5 |
| *Scotia Capital Markets 91-Day T-Bill* | *4.7* | *3.2* | *5.0* | *7.4* | *5.4* | *5.1* |
| Long-term fixed income | 8.5 | 9.2 | 12.3 | 20.4 | (2.9) | 9.3 |
| *Scotia Capital Markets Universe Bond* | *9.2* | *9.6* | *12.3* | *20.7* | *(4.3)* | *9.2* |
| Canadian equity | (3.5) | 14.7 | 29.8 | 14.4 | 2.2 | 10.9 |
| *Toronto Stock Exchange 300 Index* | *(1.6)* | *15.0* | *28.4* | *14.5* | *(0.2)* | *10.7* |
| Foreign equity | 24.7 | 15.3 | 13.0 | 16.8 | 2.8 | 14.3 |
| *Morgan Stanley (MSCI) World* | *33.5* | *20.9* | *14.0* | *17.4* | *11.3* | *19.2* |
| Real estate* | 12.8 | 20.7 | 6.4 | 7.8 | 2.9 | 9.9 |
| *Russell Canadian Property Index** | *16.1* | *18.9* | *7.0* | *5.0* | *1.9* | *9.6* |
| Overall | 7.5 | 12.4 | 16.1 | 17.2 | 0.1 | 10.5 |
| SEI median, funds over $1 billion | *8.0* | *14.9* | *18.8* | *17.4* | *(0.7)* | *11.1* |

* Real estate return is reported on a net basis after expenses while the Russell Canadian Property Index reports return on a gross basis.

# ALPHABETICAL LIST OF ENTITIES' FINANCIAL INFORMATION IN MINISTRY ANNUAL REPORTS

## ENTITIES INCLUDED IN THE CONSOLIDATED GOVERNMENT REPORTING ENTITY

| *Ministry, Department, Fund or Agency* | *Ministry Annual Report* |
|---|---|
| Agriculture Financial Services Corporation | Agriculture, Food and Rural Development |
| Alberta Agricultural Research Institute | Agriculture, Food and Rural Development |
| Alberta Alcohol and Drug Abuse Commission | Community Development |
| Alberta Dairy Control Board | Agriculture, Food and Rural Development |
| Alberta Energy and Utilities Board | Energy |
| Alberta Foundation for the Arts | Community Development |
| Alberta Gaming and Liquor Commission | Economic Development |
| Alberta Government Telephones Commission, The | Treasury |
| Alberta Heritage Foundation for Medical Research Endowment Fund | Treasury |
| Alberta Heritage Savings Trust Fund | Treasury |
| Alberta Heritage Scholarship Fund | Treasury |
| Alberta Historical Resources Foundation, The | Community Development |
| Alberta Insurance Council | Treasury |
| Alberta Motion Picture Development Corporation | Economic Development |
| Alberta Municipal Financing Corporation | Treasury |
| Alberta Oil Sands Technology and Research Authority | Science, Research and Information Technology |
| Alberta Opportunity Company | Economic Development |
| Alberta Pensions Administration Corporation | Treasury |
| Alberta Petroleum Marketing Commission | Energy |
| Alberta Research Council | Science, Research and Information Technology |
| Alberta Risk Management Fund | Treasury |
| Alberta School Foundation Fund | Education |
| Alberta Science and Research Authority | Science, Research and Information Technology |
| Alberta Securities Commission | Treasury |
| Alberta Social Housing Corporation | Municipal Affairs |
| Alberta Special Waste Management Corporation | Environmental Protection |
| Alberta Sport, Recreation, Parks and Wildlife Foundation | Community Development |
| Alberta Treasury Branches | Treasury |
| ATB Investment Services Inc. | Treasury |
| Calgary Rocky View Child and Family Services Authority | Family and Social Services |
| Chembiomed Ltd. | Treasury |
| Credit Union Deposit Guarantee Corporation | Treasury |
| Crop Reinsurance Fund of Alberta | Agriculture, Food and Rural Development |
| Department of Agriculture, Food and Rural Development | Agriculture, Food and Rural Development |
| Department of Community Development | Community Development |
| Department of Economic Development | Economic Development |
| Department of Education | Education |
| Department of Energy | Energy |
| Department of Environmental Protection | Environmental Protection |
| Department of Family and Social Services | Family and Social Services |
| Department of Justice | Justice |
| Department of Municipal Affairs | Municipal Affairs |
| Department of Public Works, Supply and Services | Public Works, Supply and Services |
| Department of Treasury | Treasury |
| Edmonton Community Board for Persons with Developmental Disabilities | Family and Social Services |
| Education Revolving Fund | Education |
| Environmental Protection and Enhancement Fund | Environmental Protection |
| Gainers Inc. | Treasury |
| Gas Alberta Operating Fund | Energy |
| Government House Foundation, The | Community Development |
| Historic Resources Fund | Community Development |
| Human Rights, Citizenship and Multiculturalism Education Fund | Community Development |
| Lottery Fund | Economic Development |
| Michener Centre Facility Board, The | Family and Social Services |
| Ministry of Advanced Education and Career Development [1] | Advanced Education and Career Development |
| Ministry of Agriculture, Food and Rural Development | Agriculture, Food and Rural Development |
| Ministry of Community Development | Community Development |

## ENTITIES INCLUDED IN THE CONSOLIDATED GOVERNMENT REPORTING ENTITY (continued)

| *Ministry, Department, Fund or Agency* | *Ministry Annual Report* |
|---|---|
| Ministry of Economic Development | Economic Development |
| Ministry of Education | Education |
| Ministry of Energy | Energy |
| Ministry of Environmental Protection | Environmental Protection |
| Ministry of Executive Council [1] | Executive Council |
| Ministry of Family and Social Services | Family and Social Services |
| Ministry of Health [1] | Health |
| Ministry of Intergovernmental and Aboriginal Affairs [1] | Intergovernmental and Aboriginal Affairs |
| Ministry of Justice | Justice |
| Ministry of Labour [1] | Labour |
| Ministry of Municipal Affairs | Municipal Affairs |
| Ministry of Public Works, Supply and Services | Public Works, Supply and Services |
| Ministry of Science, Research and Information Technology | Science, Research and Information Technology |
| Ministry of Transportation and Utilities[1] | Transportation and Utilities |
| Ministry of Treasury | Treasury |
| N.A. Properties (1994) Ltd. | Treasury |
| Natural Resources Conservation Board | Environmental Protection |
| Persons with Developmental Disabilities Calgary Region Community Board | Family and Social Services |
| Persons with Developmental Disabilities Central Alberta Community Board | Family and Social Services |
| Persons with Developmental Disabilities Foundation | Family and Social Services |
| Persons with Developmental Disabilities Northeast Alberta Community Board | Family and Social Services |
| Persons with Developmental Disabilities Northwest Alberta Community Board | Family and Social Services |
| Persons with Developmental Disabilities Provincial Board | Family and Social Services |
| Persons with Developmental Disabilities South Alberta Community Board | Family and Social Services |
| Public Works, Supply and Services Revolving Fund | Public Works, Supply and Services |
| S C Financial Ltd. | Treasury |
| Science and Research Fund | Science, Research and Information Technology |
| Utility Companies Income Tax Rebates Fund | Treasury |
| Victims of Crime Fund | Justice |
| Wild Rose Foundation, The | Community Development |

[1] Ministry includes only the department so separate department financial statements are not necessary.

## ENTITIES NOT INCLUDED IN THE CONSOLIDATED GOVERNMENT REPORTING ENTITY

| *Ministry, Department, Fund or Agency* | *Ministry Annual Report* |
|---|---|
| Alberta Cancer Board | Health |
| Alberta Heritage Foundation for Medical Research | Science, Research and Information Technology |
| Alberta Mental Health Board | Health |
| Alberta Teachers' Retirement Fund Board | Education |
| Improvement Districts Trust Account | Municipal Affairs |
| Local Authorities Pension Plan | Treasury |
| Long-Term Disability Income Continuance Plan -Bargaining Unit | Advanced Education and Career Development |
| Long-Term Disability Income Continuance Plan -Management, Opted Out and Excluded | Advanced Education and Career Development |
| Management Employees Pension Plan | Treasury |
| Provincial Judges and Masters in Chambers Pension Plan | Treasury |
| Public Post Secondary Institutions | Advanced Education and Career Development |
| Public Service Management (Closed Membership) Pension Plan | Treasury |
| Public Service Pension Plan | Treasury |
| Regional Health Authorities | Health |
| School Boards | Education |
| 771045 Alberta Ltd. operating as Travel Alberta | Economic Development |
| Special Areas Trust Account | Municipal Affairs |
| Special Forces Pension Plan | Treasury |
| Universities Academic Pension Plan | Treasury |
| Workers' Compensation Board | Labour |

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